Revised Legislative Proposals and Explanatory Notes on Trusts

Published by
The Honourable Paul Martin, P.C., M.P.
Minister of Finance

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Legislative Proposals

INCOME TAX ACT

1. (1) The definition "disposition of property" in subsection 13(21) of the *Income Tax Act* is repealed.

(2) Subsection (1) applies to transactions and events that occur after December 23, 1998.

2. (1) Clause 40(2)(*g*)(iv)(A) of the Act is replaced by the following:

(A) a trust governed by a deferred profit sharing plan, an employees profit sharing plan or a registered retirement income fund under which the taxpayer is a beneficiary or immediately after the disposition becomes a beneficiary, or

(2) Subsection (1) applies to the 1998 and subsequent taxation years.

3. (1) Section 43 of the Act is replaced by the following:

General rule for part dispositions

43. (1) For the purpose of computing a taxpayer's gain or loss for a taxation year from the disposition of part of a property, the adjusted cost base to the taxpayer, immediately before the disposition, of that part is the portion of the adjusted cost base to the taxpayer at that time of the whole property that can reasonably be regarded as attributable to that part.

Payments out of trust income, etc.

(2) Notwithstanding subsection (1), where part of a capital interest of a taxpayer in a trust would, but for paragraph (*g*) or (*h*) of the definition "disposition" in subsection 248(1), be disposed of solely because of the satisfaction of a right to enforce a payment from the trust, no part of the adjusted cost base to the taxpayer of the taxpayer's capital interest in the trust shall be allocated to that part of the capital interest.

(2) Subsection 43(1) of the Act, as enacted by subsection (1), applies to dispositions that occur after 1999.

(3) Subsection 43(2) of the Act, as enacted by subsection (1), applies to satisfactions of rights that occur after 1999.

4. (1) Paragraph 49(5)(*b*) of the Act is replaced by the following:

(*b*) for the purposes of subsections (2) to (4) and subparagraph (*b*)(iv) of the definition "disposition" in subsection 248(1), the original option and each extension or renewal of it is deemed to be the same option; and

(2) Subsection (1) applies to options granted after December 23, 1998.

5. (1) Subsections 52(1) and (1.1) of the Act are replaced by the following:

Cost of certain property the value of which included in income

52. (1) Where

(*a*) a taxpayer acquired property after 1971 (other than an annuity contract, a right as a beneficiary under a trust to enforce payment to the taxpayer by the trust, property acquired in circumstances to which subsection (2) or (3) applies or property acquired from a trust in satisfaction of all or part of the taxpayer's capital interest in the trust), and

(*b*) an amount in respect of its value was

(i) included, otherwise than under section 7, in computing

(A) the taxpayer's taxable income or taxable income earned in Canada, as the case may be, for a taxation year during which the taxpayer was non-resident, or

(B) the taxpayer's income for a taxation year throughout which the taxpayer was resident in Canada, or

(ii) for the purpose of computing the tax payable under Part XIII by the taxpayer, included in an amount that was paid or credited to the taxpayer,

for the purposes of this subdivision, the amount so included shall be added in computing the cost to the taxpayer of the property, except to the extent that such amount was otherwise added to the cost or included in computing the adjusted cost base to the taxpayer of the property.

(2) Subsection 52(6) of the Act is repealed.

(3) Subsection (1) applies after 1999 except that, in respect of property acquired before 2000 and disposed of before March 2000, paragraph 52(1)(*a*) of the Act, as enacted by that subsection, shall be read as follows:

(*a*) a taxpayer acquired property after 1971 (other than an annuity contract or property acquired as described in subsection (2), (3) or (6)), and

(4) Subsection (2) applies after 1999, but not to rights that were acquired before 2000 that are disposed of before March 2000.

6. (1) The portion of paragraph 53(2)(*h*) of the Act before subparagraph (i) is replaced by the following:

(*h*) where the property is a capital interest of the taxpayer in a trust (other than an interest in a personal trust that has never been acquired for consideration or an interest of a taxpayer in a trust described in any of paragraphs (*a*) to (*e*.1) of the definition "trust" in subsection 108(1)),

(2) The portion of paragraph 53(2)(*i*) of the Act before subparagraph (i) is replaced by the following:

(*i*) where the property is a capital interest in a trust (other than a unit trust) not resident in Canada that was purchased after 1971 and before that time by the taxpayer from a non-resident person at a time (in this paragraph referred to as the "purchase time") when the property was not taxable Canadian property and the fair market value of such of the trust property as was

(3) The portion of paragraph 53(2)(*i*) of the Act after subparagraph (v) is replaced by the following:

was not less than 50% of the fair market value of all the trust property, that proportion of the amount, if any, by which

(vi) the fair market value at the purchase time of such of the trust properties as were properties described in any of subparagraphs (i) to (v)

exceeds

(vii) the total of the cost amounts to the trust at the purchase time of such of the trust properties as were properties described in any of subparagraphs (i) to (v),

that the fair market value at the purchase time of the interest is of the fair market value at the purchase time of all capital interests in the trust;

(4) The portion of paragraph 53(2)(*j*) of the Act before subparagraph (i) is replaced by the following:

(*j*) where the property is a unit of a unit trust not resident in Canada that was purchased after 1971 and before that time by the taxpayer from a non-resident person at a time (in this paragraph referred to as the "purchase time") when the property was not taxable Canadian property and the fair market value of such of the trust property as was

(5) The portion of paragraph 53(2)(*j*) of the Act after subparagraph (v) is replaced by the following:

was not less than 50% of the fair market value of all the trust property, that proportion of the amount, if any, by which

(vi) the fair market value at the purchase time of such of the trust properties as were properties described in any of subparagraphs (i) to (v)

exceeds

(vii) the total of the cost amounts to the trust at the purchase time of such of the trust properties as were properties described in any of subparagraphs (i) to (v),

that the fair market value at the purchase time of the unit is of the fair market value at the purchase time of all the issued units of the trust;

(6) The portion of subsection 53(4) of the Act before paragraph (*a*) is replaced by the following:

Recomputation of adjusted cost base on transfers and deemed dispositions

(4) Where at any time in a taxation year a person or partnership (in this subsection referred to as the "vendor") disposes of a specified property and the proceeds of disposition of the property are determined under paragraph 48.1(1)(*c*), section 70 or 73, subsection 85(1), paragraph 87(4)(*a*) or (*c*) or 88(1)(*a*), subsection 97(2) or 98(2),

paragraph 98(3)(*f*) or (5)(*f*), subsection 104(4), paragraph 107(2)(*a*), (2.1)(*a*), (4)(*d*) or (5)(*a*), 107.4(3)(*a*) or 111(4)(*e*) or section 128.1,

(7) Subsection (1) applies to amounts that become payable after 1999.

(8) Subsections (2) to (5) apply for the purpose of computing the adjusted cost base of property after April 26, 1995.

(9) Subsection (6) applies to the 1998 and subsequent taxation years.

7. (1) The definition "disposition" in section 54 of the Act is repealed.

(2) Subsection (1) applies to transactions and events that occur after December 23, 1998.

8. (1) Subsection 59(5) of the Act is replaced by the following:

Definition of "proceeds of disposition"

(5) In this section, "proceeds of disposition" has the meaning assigned by section 54.

(2) Subsection (1) applies to transactions and events that occur after December 23, 1998.

9. (1) The definitions "disposition" and "proceeds of disposition" in subsection 66.4(5) of the Act are replaced by the following:

"proceeds of disposition"
« produit de disposition »

"proceeds of disposition" has the meaning assigned by section 54.

(2) Subsection (1) applies to transactions and events that occur after December 23, 1998.

10. (1) Paragraph 69(1)(*b*) of the Act is amended by striking out the word "or" at the end of subparagraph (i), by adding the word "or" at the end of subparagraph (ii) and by adding the following after subparagraph (ii):

(iii) to a trust because of a disposition of a property that does not result in a change in the beneficial ownership of the property,

(2) Paragraph 69(1)(*c*) of the Act is replaced by the following:

(*c*) where a taxpayer acquires a property by way of gift, bequest or inheritance or because of a disposition that does not result in a change in the beneficial ownership of the property, the taxpayer is deemed to acquire the property at its fair market value.

(3) Subsection (1) applies to dispositions that occur after December 23, 1998.

(4) Subsection (2) applies to acquisitions that occur after December 23, 1998.

11. (1) Subsection 70(5.3) of the Act is replaced by the following:

Fair market value

(5.3) For the purposes of subsections (5) and 104(4) and section 128.1, the fair market value at any time of any property deemed to have been disposed of at that time as a consequence of an individual's death or as a consequence of the individual becoming or ceasing to be resident in Canada shall be determined as though the fair market value at that time of any life insurance policy under which the individual was the person whose life was insured were the cash surrender value (as defined in subsection 148(9)) of the policy immediately before the individual died or became or ceased to be resident in Canada, as the case may be.

(2) The portion of subsection 70(9.1) of the Act before paragraph (*a*) is replaced by the following:

Transfer of farm property from spouse's trust to settlor's children

(9.1) Where any property in Canada of a taxpayer that is land or depreciable property of a prescribed class has been transferred or distributed to a trust described in subsection (6) or subsection 73(1) (as that subsection applied to transfers before 2000) or a trust to which subparagraph 73(1.01)(*c*)(i) applies and the property or a replacement property for that property in respect of which the trust has made an election under subsection 13(4) or 44(1) was, immediately before the death of the taxpayer's spouse who was a beneficiary under the trust, used in the business of farming and has, on the death of the spouse and

as a consequence of the death, been transferred or distributed to and become vested indefeasibly in a child of the taxpayer who was resident in Canada immediately before the death of the spouse, the following rules apply:

(3) The portion of subsection 70(9.3) of the Act before paragraph (a) is replaced by the following:

Transfer of family farm corporation or partnership from spouse's trust to children of settlor

(9.3) Where property of a taxpayer has been transferred or distributed to a trust described in subsection (6) or 73(1) (as that subsection applied to transfers before 2000) or a trust to which subparagraph 73(1.01)(c)(i) applies and the property was,

(4) Subsection (1) applies to dispositions that occur after October 1, 1996.

(5) Subsections (2) and (3) apply to transfers and distributions to children that occur after 1999.

12. (1) Subsections 73(1) and (1.1) of the Act are replaced by the following:

***Inter vivos* transfers by individuals**

73. (1) For the purposes of this Part, where at any time any particular capital property of an individual (other than a trust) has been transferred in circumstances to which subsection (1.01) applies and both the individual and the transferee would, if this Act were read without reference to any provision that can deem a trust to be resident in Canada, be resident in Canada at that time, unless the individual elects in the individual's return of income under this Part for the taxation year in which the property was transferred not to have the provisions of this subsection apply, the particular property is deemed

(*a*) to have been disposed of at that time by the individual for proceeds equal to,

(i) where the particular property is depreciable property of a prescribed class, that proportion of the undepreciated capital cost to the individual immediately before that time of all property of that class that the fair market value immediately before that time

of the particular property is of the fair market value immediately before that time of all of that property of that class, and

(ii) in any other case, the adjusted cost base to the individual of the particular property immediately before that time; and

(*b*) to have been acquired at that time by the transferee for an amount equal to those proceeds.

Qualifying transfers

(1.01) Subject to subsection (1.02), property is transferred by an individual in circumstances to which this subsection applies where it is transferred to

(*a*) the individual's spouse;

(*b*) a former spouse of the individual in settlement of rights arising out of their marriage; or

(*c*) a trust created by the individual under which

(i) the individual's spouse is entitled to receive all of the income of the trust that arises before the spouse's death and no person except the spouse may, before the spouse's death, receive or otherwise obtain the use of any of the income or capital of the trust,

(ii) the individual is entitled to receive all of the income of the trust that arises before the individual's death and no person except the individual may, before the individual's death, receive or otherwise obtain the use of any of the income or capital of the trust, or

(iii) the individual or the individual's spouse is, in combination with the other, entitled to receive all of the income of the trust that arises before the later of the death of the individual and the death of the spouse and no other person may, before the later of those deaths, receive or otherwise obtain the use of any of the income or capital of the trust.

Exception for transfers

(1.02) Subsection (1.01) applies to a transfer of property by an individual to a trust the terms of which satisfy the conditions in subparagraph (1.01)(*c*)(ii) or (iii) only where

(*a*) the trust was created after 1999;

(*b*) either

(i) the individual has attained 65 years of age at the time of the creation of the trust, or

(ii) no person (other than the individual) or partnership has any absolute or contingent right as a beneficiary under the trust (determined with reference to subsection 104(1.1)); and

(*c*) unless subparagraph (*b*)(ii) applies in respect of the transfer, the transfer is not part of a series of transactions or events

(i) that includes a transfer of property to the individual (or the spouse or former spouse of the individual) from a trust (other than a testamentary trust) in circumstances to which subsection 107(2) applied, and

(ii) one of the main purposes of which can reasonably be considered to be to avoid the application of subsection 104(4) or (5) on a day determined under paragraph 104(4)(*b*) or (*c*).

Interpretation

(1.1) For greater certainty, where, under the laws of a province or because of a decree, order or judgment of a competent tribunal made in accordance with those laws, a particular individual

(*a*) acquires or is deemed to have acquired,

(*b*) is deemed or declared to have or is awarded, or

(*c*) has vested in the particular individual,

property that was or would, but for those provisions, have been a capital property of the individual referred to in subsection (1), that property is, for the purposes of that subsection and subsection (1.01), deemed to be capital property of the individual referred to in subsection (1) that has been transferred to the particular individual.

(2) Subsection (1) applies to transfers that occur after 1999.

13. (1) Paragraph 75(3)(*a*) of the Act is replaced by the following:

(*a*) by a trust governed by a deferred profit sharing plan, an employee benefit plan, an employees profit sharing plan, a registered education savings plan, a registered pension plan, a registered

retirement income fund, a registered retirement savings plan, a registered supplementary unemployment benefit plan or a retirement compensation arrangement;

(2) Paragraph 75(3)(*a*) of the Act, as enacted by subsection (1), applies to taxation years that end after October 8, 1986 and, notwithstanding subsection 152(4) to (5) of the Act, the Minister of National Revenue shall make such assessments, reassessments and additional assessments of tax, interest and penalties as are necessary to give effect to the words "retirement compensation arrangement" in that paragraph.

14. (1) Clause 94(1)(*c*)(i)(B) of the Act is replaced by the following:

(B) the amount that would be the foreign accrual property income for the year of the trust if

(I) except for the purpose of applying subsections 104(4) to (5.2) to days after 1998 that are determined under subsection 104(4), the trust were a non-resident corporation all the shares of which were owned by a person who was resident in Canada,

(II) the description of A in the definition "foreign accrual property income" in subsection 95(1) were, in respect of dividends received after 1998, read without reference to paragraph (*b*) of that subsection,

(III) the descriptions of B and E in that definition were, in respect of dispositions that occur after 1998, read without reference to "other than dispositions of excluded property to which none of paragraphs (2)(*c*), (*d*) and (*e*) apply",

(IV) the value of C in that definition were nil, and

(V) for the purpose of computing the trust's foreign accrual property income, the consequences of the application of subsections 104(4) to (5.2) applied in respect of days after 1998 that are determined under subsection 104(4),

(2) Subparagraph 94(1)(*c*)(i) of the Act is amended by adding the following after clause (C):

(D) the amount, if any, required by section 94.1 to be included in computing its income for the year, and

(3) Subsections (1) and (2) apply to the 1999 and subsequent taxation years.

15. (1) Subsection 104(1) of the Act is replaced by the following:

Reference to trust or estate

104. (1) In this Act, a reference to a trust or estate (in this subdivision referred to as a "trust") shall, unless the context otherwise requires, be read to include a reference to the trustee or the executor, administrator, heir or other legal representative having ownership or control of the trust property, but a trust is, for the purposes of all provisions of this Act other than this subsection and subsection (1.1), deemed not to include an arrangement under which the trust can reasonably be considered to act as agent for all the beneficiaries under the trust with respect to all dealings with all of the trust's property unless the trust is described in any of paragraphs (*a*) to (*e*.1) of the definition "trust" in subsection 108(1).

Restricted meaning of "beneficiary"

(1.1) For the purposes of subsection (1), subparagraph 73(1.02)(*b*)(ii) and paragraph 107.4(1)(*e*), a person or partnership is deemed not to be a beneficiary under a trust at a particular time where the person or partnership is beneficially interested in the trust at the particular time solely because of

(*a*) a right that may arise as a consequence of the terms of the will or other testamentary instrument of an individual who, at the particular time, is a beneficiary under the trust;

(*b*) a right that may arise as a consequence of the law governing the intestacy of an individual;

(*c*) a right as a shareholder under the terms of the shares of the capital stock of a corporation that, at the particular time, is a beneficiary under the trust;

(*d*) a right as a member of a partnership under the terms of the partnership agreement, where, at the particular time, the partnership is a beneficiary under the trust; or

(*e*) any combination of rights described in paragraphs (*a*) to (*d*).

(2) The portion of subsection 104(4) of the Act before paragraph (*a*) is replaced by the following:

Deemed disposition by trust

(4) Every trust is, at the end of each of the following days, deemed to have disposed of each property of the trust (other than exempt property) that was capital property (other than excluded property or depreciable property) or land included in the inventory of a business of the trust for proceeds equal to its fair market value (determined with reference to subsection 70(5.3)) at the end of that day and to have reacquired the property immediately thereafter for an amount equal to that fair market value, and for the purposes of this Act those days are

(3) Paragraph 104(4)(*a*) of the Act is amended by striking out the word "or" at the end of subparagraph (i.1), by adding the word "or" at the end of subparagraph (ii) and by replacing the portion after subparagraph (ii) by the following:

(ii.1) is a trust created after 1999 by a taxpayer during the taxpayer's lifetime that, at any time after 1999, was a trust

under which

(iii) the taxpayer's spouse was entitled to receive all of the income of the trust that arose before the spouse's death and no person except the spouse could, before the spouse's death, receive or otherwise obtain the use of any of the income or capital of the trust, or

(iv) in the case of a trust described in subparagraph (ii.1) created by a taxpayer who had attained 65 years of age at the time the trust was created,

(A) the taxpayer was entitled to receive all of the income of the trust that arose before the taxpayer's death and no person except the taxpayer could, before the taxpayer's death, receive or otherwise obtain the use of any of the income or capital of the trust, or

(B) the taxpayer or the taxpayer's spouse was, in combination with the spouse or the taxpayer, as the case may be, entitled to receive all of the income of the trust that arose before the later of the death of the taxpayer and the death of the spouse and no other person could, before the later of those deaths, receive or otherwise obtain the use of any of the income or capital of the trust,

the day on which the death or the later death, as the case may be, occurs;

(4) Subsection 104(4) of the Act is amended by adding the following after paragraph (*a*.1):

(*a*.2) where the trust makes a distribution to a beneficiary in respect of the beneficiary's capital interest in the trust, the distribution can reasonably be considered to have been financed by a liability of the trust and one of the purposes of incurring the liability was to avoid taxes otherwise payable under this Part as a consequence of the death of any individual, the day on which the distribution is made (determined as if a day ends for the trust immediately after the time at which each distribution is made by the trust to a beneficiary in respect of the beneficiary's capital interest in the trust);

(*a*.3) where property (other than property described in any of subparagraphs 128.1(4)(*b*)(i) to (iii)) has been transferred by a taxpayer after **ANNOUNCEMENT DATE** to the trust in circumstances to which subsection 73(1) applies, it is reasonable to conclude that the property was so transferred in anticipation that the taxpayer would subsequently cease to reside in Canada and the taxpayer subsequently ceases to reside in Canada, the first day after that transfer during which the taxpayer ceases to reside in Canada (determined as if a day ends for the trust immediately after each time at which the taxpayer ceases to be resident in Canada);

(5) Paragraph 104(4)(*c*) of the Act is replaced by the following:

(*c*) the day that is 21 years after any day (other than a day determined under paragraph (*a*), (*a*.1), (*a*.2) or (*a*.3)) that is, because of this subsection, a day on which the trust is deemed to have disposed of each such property.

(6) The portion of subsection 104(5) of the Act before paragraph (*a*) is replaced by the following:

Depreciable property

(5) Every trust is, at the end of each day determined under subsection (4) in respect of the trust, deemed to have disposed of each property of the trust (other than exempt property) that was a depreciable property of a prescribed class of the trust for proceeds equal to its fair market value at the end of that day and to have reacquired the property immediately after that day at a capital cost (in this subsection referred to as the "deemed capital cost") equal to that fair market value, except that

(7) The portion of subsection 104(5.2) of the Act before paragraph (*b*) is replaced by the following:

Resource property

(5.2) Where at the end of a day determined under subsection (4) in respect of a trust the trust owns a Canadian resource property (other than an exempt property) or a foreign resource property (other than an exempt property),

(*a*) for the purpose of determining the amounts under subsection 59(1), paragraph 59(3.2)(*c*), subsections 66(4) and 66.2(1), the definition "cumulative Canadian development expense" in subsection 66.2(5), subsection 66.4(1) and the definition "cumulative Canadian oil and gas property expense" in subsection 66.4(5), the trust is deemed

(i) to have a taxation year (in this subsection referred to as the "old taxation year") that ended at the end of that day and a new taxation year (in this subsection referred to as the "new taxation year") that begins immediately after that day, and

(ii) to have disposed, immediately before the end of the old taxation year, of each of those properties for proceeds that became receivable at that time equal to its fair market value at that time and to have reacquired, at the beginning of the new taxation year, each such property for an amount equal to that fair market value; and

(8) Subsection 104(5.3) of the Act is amended by adding the word "and" at the end of paragraph (*b*.1) and by replacing the portion of paragraph (*c*) before subparagraph (i) with the following:

(*c*) subsection 107.4(3) does not apply to a disposition by the trust during the period

(9) Subsection 104(5.3) of the Act is amended by striking out the word "and" at the end of paragraph (*c*) and by repealing paragraph (*d*).

(10) The portion of subsection 104(5.8) of the Act before paragraph (*a*) is replaced by the following:

Trust transfers

(5.8) Where capital property (other than excluded property), land included in inventory, Canadian resource property or foreign resource property is transferred at a particular time by a trust (in this subsection referred to as the "transferor trust") to another trust (in this subsection referred to as the "transferee trust") in circumstances

in which subsection 107(2) or 107.4(3) or paragraph (*f*) of the definition "disposition" in subsection 248(1) applies,

(11) The portion of subparagraph 104(5.8)(*a*)(i) of the Act before clause (A) is replaced by the following:

(i) subject to paragraphs (*b*) to (*b*.2), the first day (in this subsection referred to as the "disposition day") ending at or after the particular time that would, if this section were read without reference to paragraph (4)(*a*.2) and (*a*.3), be determined in respect of the transferee trust is deemed to be the earliest of

(12) Clause 104(5.8)(*a*)(i)(C) of the Act is replaced by the following:

(C) the first day that ends at or after the particular time, where

(I) the transferor trust is a joint spousal trust, a post-1971 spousal trust or a trust described in the definition "pre-1972 spousal trust" in subsection 108(1), and

(II) the spouse referred to in paragraph (4)(*a*) or that definition is alive at the particular time,

(C.1) the first day that ends at or after the particular time, where

(I) the transferor trust is an *alter ego* trust or joint spousal trust; and

(II) the taxpayer referred to in paragraph (4)(*a*) is alive at the particular time,

(13) Paragraph 104(5.8)(*b*) of the Act is replaced by the following:

(*b*) paragraph (*a*) does not apply in respect of the transfer where

(i) the transferor trust is a post-1971 spousal trust or a trust described in the definition "pre-1972 spousal trust" in subsection 108(1),

(ii) the spouse referred to in paragraph (4)(*a*) or that definition is alive at the particular time, and

(iii) the transferee trust is a post-1971 spousal trust or a trust described in the definition "pre-1972 spousal trust" in subsection 108(1);

(*b*.1) paragraph (*a*) does not apply in respect of the transfer where

(i) the transferor trust is an *alter ego* trust,

(ii) the taxpayer referred to in paragraph (4)(*a*) is alive at the particular time, and

(iii) the transferee trust is an *alter ego* trust;

(*b*.2) paragraph (*a*) does not apply in respect of the transfer where

(i) the transferor trust is a joint spousal trust,

(ii) either the taxpayer or spouse referred to in paragraph (4)(*a*) is alive at the particular time, and

(iii) the transferee trust is a joint spousal trust; and

(14) Subsection 104(6) is amended by striking out the word "and" at the end of paragraph (*a*.2) and by adding the following after paragraph (*a*.2):

(*a*.3) in the case of an *inter vivos* trust deemed by subsection 143(1) to exist in respect of a congregation that is a constituent part of a religious organization, such part of its income for the year as became payable in the year to a beneficiary; and

(15) Clauses 104(6)(*b*)(ii)(A) and (B) are replaced by the following:

(A) is a post-1971 spousal trust that was created after December 20, 1991, or

(B) would be a post-1971 spousal trust if the reference in paragraph (4)(*a*) to "at the time it was created" were read as "on December 20, 1991",

(16) Paragraph 104(6)(*b*) of the Act is amended by striking out the word "and" at the end of subparagraph (ii) and by replacing subparagraph 104(6)(*b*)(iii) of the Act by the following:

(ii.1) where the trust is an *alter ego* trust or a joint spousal trust and the death or later death, as the case may be, referred to in subparagraph (4)(*a*)(iv) has not occurred before the end of the

year, such part of the amount that, but for this subsection and subsections (12), 12(10.2) and 107(4), would be its income as became payable in the year to a beneficiary (other than a taxpayer or a spouse referred to in clause (4)(*a*)(iv)(A) or (B)) or was included under subsection 105(2) in computing the income of a beneficiary (other than such a taxpayer or spouse), and

(iii) where the trust is an *alter ego* trust, a joint spousal trust or a post-1971 spousal trust and the death or the later death, as the case may be, referred to in paragraph (4)(*a*) in respect of the trust occurred on a day in the year, the amount, if any, by which

(A) the maximum amount that would be deductible under this subsection in computing the trust's income for the year if this subsection were read without reference to this subparagraph

exceeds the total of

(B) the amount that, but for this subsection and subsections (12), 12(10.2) and 107(4), would be its income as became payable in the year to the taxpayer or spouse referred to in subparagraph (4)(*a*)(iii) or clause (4)(*a*)(iv)(A) or (B), as the case may be, and

(C) the amount that would be the trust's income for the year if that income were computed without reference to this subsection and subsection (12) and as if the year began immediately after the end of the day,

(17) Subsection 104(13) of the Act is replaced by the following:

Income of beneficiary

(13) There shall be included in computing the income for a particular taxation year of a beneficiary under a trust such of the following amounts as are applicable:

(*a*) in the case of a trust (other than a trust referred to in paragraph (*a*) of the definition "trust" in subsection 108(1)), such part of the amount that, but for subsections (6) and (12), would be the trust's income for the trust's taxation year that ended in the particular year as became payable in the trust's year to the beneficiary; and

(*b*) in the case of a trust governed by an employee benefit plan to which the beneficiary has contributed as an employer, such part of the amount that, but for subsections (6) and (12), would be the

trust's income for the trust's taxation year that ended in the particular year as was paid in the trust's year to the beneficiary.

(18) Paragraphs 104(15)(*a*) and (*b*) of the Act are replaced by the following:

(*a*) where the trust is an *alter ego* trust, a joint spousal trust, a post-1971 spousal trust or a trust described in the definition "pre-1972 spousal trust" in subsection 108(1) at the end of the year and a beneficiary, referred to in paragraph (4)(*a*) or in that definition, is alive at the end of the year, an amount equal to

(i) if the preferred beneficiary is a beneficiary so referred to, the trust's accumulating income for the year, and

(ii) in any other case, nil;

(*b*) where paragraph (*a*) does not apply and the preferred beneficiary's interest in the trust is not solely contingent on the death of another beneficiary who has a capital interest in the trust and who does not have an income interest in the trust, the trust's accumulating income for the year; and

(19) The portion of subsection 104(19) of the Act after paragraph (*b*) is replaced by the following:

if so designated by the trust in respect of the beneficiary in its return of income for the year, is deemed, for the purposes of paragraphs 82(1)(*b*) and 107(1)(*c*) and (*d*) and section 112, not to have been received by the trust, and for the purposes of this Act (other than Part XIII), to be a taxable dividend on the share received by the beneficiary in the particular year from the corporation.

(20) Subsection (1) applies to the 1998 and subsequent taxation years, except that in connection with transfers of property that occur before December 24, 1998, subsection 104(1) of the Act, as enacted by subsection (1), shall be read as follows:

Reference to trust or estate

104. (1) In this Act, a reference to a trust or estate (in this subdivision referred to as a "trust") shall, unless the context otherwise requires, be read to include a reference to the trustee or the executor, administrator, heir or other legal representative having ownership or control of the trust property.

(21) Subsection (2) applies to days after December 23, 1998 that are determined in respect of a trust under subsection 104(4) of the *Income Tax Act*, as enacted by section 15 of this Act, and for the purpose of determining the cost amount to a trust after December 23, 1998 of property to days after 1992 that are determined in respect of the trust under subsection 104(4) of the *Income Tax Act*, as enacted by section 15 of this Act.

(22) Subsections (3) and (5) and (15) to (17) apply to the 2000 and subsequent taxation years.

(23) Subsection (4) applies to days after ANNOUNCEMENT DATE that are determined under subsection 104(4) of the *Income Tax Act*, as enacted by section 15 of by this Act.

(24) Subsections (6) and (7) apply to days after December 23, 1998 that are determined under subsection 104(4) of the *Income Tax Act*, as enacted by section 15 of this Act.

(25) Subsections (8) and (9) apply to transfers made after December 23, 1998.

(26) Subsection (10) applies to transfers made after February 11, 1991 except that, for transfers made before December 24, 1998, the portion of subsection 104(5.8) of the Act before paragraph (*a*), as enacted by subsection (10), shall be read as follows:

(5.8) Where capital property (other than excluded property), land included in inventory, Canadian resource property or foreign resource property is transferred at a particular time by a trust (in this subsection referred to as the "transferor trust") to another trust (in this subsection referred to as the "transferee trust") in circumstances in which paragraph (*e*) of the definition "disposition" in section 54 or subsection 107(2) applies and the transferee trust is not described in paragraph (*g*) of the definition "trust" in subsection 108(1),

(27) Subsection (11) applies to transfers made after ANNOUNCEMENT DATE.

(28) Subsections (12) and (13) apply to transfers made after 1999.

(29) Subsection (14) applies to the 1998 and subsequent taxation years.

(30) Subsection (18) applies to the 2000 and subsequent taxation years.

(31) Subsection (19) applies to taxation years that end after 2000.

16. (1) Subsection 106(1.1) of the Act is replaced by the following:

Cost of income interest in a trust

(1.1) The cost to a taxpayer of an income interest of the taxpayer in a trust is deemed to be nil unless

(*a*) any part of the interest was acquired by the taxpayer from a person who was the beneficiary in respect of the interest immediately before that acquisition; or

(*b*) the cost of any part of the interest would otherwise be determined not to be nil under paragraph 128.1(1)(*c*) or (4)(*c*).

(2) Subsection (1) applies to the 2000 and subsequent taxation years.

17. (1) The portion of paragraph 107(1)(*a*) of the Act before subparagraph (i) is replaced by the following:

(*a*) where the trust is a personal trust or a prescribed trust, for the purpose of computing the taxpayer's capital gain, if any, from the disposition, the adjusted cost base to the taxpayer of the interest or the part of the interest, as the case may be, immediately before the disposition is, unless any part of the interest has ever been acquired for consideration and, at the time of the disposition, the trust would be non-resident if this Act were read without reference to subparagraph 94(1)(*c*)(i), deemed to be the greater of

(2) Paragraph 107(1)(*b*) of the Act is repealed.

(3) The portion of subsection 107(1) of the Act after paragraph (*d*) is repealed.

(4) Subsection 107(1.1) of the Act is replaced by the following:

Cost of capital interest in a trust

(1.1) The cost to a taxpayer of a capital interest of the taxpayer in a personal trust or a prescribed trust is deemed to be,

(*a*) where the taxpayer elected under subsection 110.6(19) in respect of the interest and the trust does not elect under that subsection in respect of any property of the trust, the taxpayer's cost of the interest determined under paragraph 110.6(19)(*a*); and

(*b*) in any other case, nil, unless

(i) any part of the interest was acquired by the taxpayer from a person who was the beneficiary in respect of the interest immediately before that acquisition, or

(ii) the cost of any part of the interest would otherwise be determined not to be nil under section 48 as it read in its application before 1993, paragraph 111(4)(*e*) or 128.1(1)(*c*) or (4)(*c*).

(5) The portion of subsection 107(2) of the Act before paragraph (*a*) is replaced by the following:

Distribution by personal trust

(2) Subject to subsection (2.001), where at any time a property of a personal trust or a prescribed trust is distributed by the trust to a taxpayer who was a beneficiary under the trust in satisfaction of all or any part of the taxpayer's capital interest in the trust,

(6) The portion of subsection 107(2) of the Act before paragraph (*a*), as enacted by subsection (5), is replaced by the following:

Distribution by personal trust

(2) Subject to subsections (2.001) and (2.002) and (4) to (5), where at any time a property of a personal trust or a prescribed trust is distributed by the trust to a taxpayer who was a beneficiary under the trust and there is a resulting disposition of all or any part of the taxpayer's capital interest in the trust,

(7) Paragraphs 107(2)(*b*) and (*c*) of the Act are replaced by the following:

(*b*) subject to subsection (2.2), the taxpayer is deemed to have acquired the property at a cost equal to the total of its cost amount to the trust immediately before that time and the specified percentage of the amount, if any, by which

(i) the adjusted cost base to the taxpayer of the capital interest or part thereof, as the case may be, immediately before that time (determined without reference to paragraph (1)(*a*))

exceeds

(ii) the cost amount to the taxpayer of the capital interest or part thereof, as the case may be, immediately before that time;

(*b*.1) for the purpose of paragraph (*b*), the specified percentage is,

(i) where the property is capital property (other than depreciable property), 100%,

(ii) where the property is eligible capital property in respect of a business of the trust, 100%, and

(iii) in any other case, 75%;

(*c*) the taxpayer is deemed to have disposed of all or part, as the case may be, of the capital interest for proceeds equal to the amount, if any, by which

(i) the cost at which the taxpayer would be deemed by paragraph (*b*) to have acquired the property if the specified percentage referred to in that paragraph were 100%

exceeds

(ii) the total of all amounts each of which is an eligible offset at that time of the taxpayer in respect of the capital interest or the part of it;

(8) Subsection 107(2) of the Act is amended by adding the following after paragraph (*d*):

(*d*.1) where

(i) the taxpayer is non-resident at that time,

(ii) that time is before October 2, 1996, and

(iii) the property was deemed by paragraph 51(1)(*f*), 85(1)(*i*) or 85.1(1)(*a*), subsection 87(4) or (5) or paragraph 97(2)(*c*) to be taxable Canadian property of the trust,

the property is deemed to be taxable Canadian property of the taxpayer;

(9) Section 107 of the Act is amended by adding the following after subsection (2):

No rollover on election by a trust

(2.001) Where a trust makes a distribution of a property to a beneficiary of the trust in full or partial satisfaction of the beneficiary's capital interest in the trust and so elects in prescribed form filed with the Minister with the trust's return of income for its taxation year in which the distribution occurred, subsection (2) does not apply to the distribution if

(*a*) the trust is resident in Canada at the time of the distribution;

(*b*) the property is taxable Canadian property; or

(*c*) the property is capital property used in, eligible capital property in respect of, or property described in the inventory of, a business carried on by the trust through a permanent establishment (as defined by regulation) in Canada immediately before the time of the distribution.

No rollover on election by a beneficiary

(2.002) Where a non-resident trust makes a distribution of a property (other than a property described in paragraph (2.001)(*b*) or (*c*)) to a beneficiary of the trust in full or partial satisfaction of the beneficiary's capital interest in the trust and the beneficiary makes an election under this subsection in prescribed form filed with the Minister with the beneficiary's return of income for the beneficiary's taxation year in which the distribution occurred,

(*a*) subsection (2) does not apply to the distribution; and

(*b*) for the purpose of subparagraph (1)(*a*)(ii), the cost amount of the interest to the beneficiary is deemed to be nil.

(10) The portion of subsection 107(2.01) of the Act before paragraph (*a*) is replaced by the following:

Distribution of principal residence

(2.01) Where property that would, if a personal trust had designated the property under paragraph (*c*.1) of the definition "principal residence" in section 54, be a principal residence (within the meaning of that definition) of the trust for a taxation year, is at any time (in this subsection referred to as "that time") distributed by the trust to a

taxpayer in circumstances to which subsection (2) applies and the trust so elects in its return of income for the taxation year that includes that time,

(11) Subsection 107(2.1) of the Act is replaced by the following:

Other distributions

(2.1) Where at any time a property of a trust is distributed by the trust to a beneficiary under the trust, there would, if this Act were read without reference to paragraphs (*g*) and (*h*) of the definition "disposition" in subsection 248(1), be a resulting disposition of all or any part of the beneficiary's capital interest in the trust (which interest or part, as the case may be, is in this subsection referred to as the "former interest") and the rules in subsection (2) and section 132.2 do not apply in respect of the distribution,

(*a*) the trust is deemed to have disposed of the property for proceeds equal to its fair market value at that time;

(*b*) the beneficiary is deemed to have acquired the property at a cost equal to the proceeds determined under paragraph (*a*);

(*c*) the beneficiary's proceeds of disposition of the portion of the former interest disposed of by the beneficiary on the distribution are deemed to be equal to the amount, if any, by which

(i) the proceeds determined under paragraph (*a*) (other than the portion, if any, of the proceeds that is a payment to which paragraph (*g*) or (*h*) of the definition "disposition" in subsection 248(1) applies),

exceeds the total of

(ii) where the property is not a Canadian resource property or foreign resource property, the amount, if any, by which

(A) the fair market value of the property at that time

exceeds the total of

(B) the cost amount to the trust of the property immediately before that time, and

(C) the portion, if any, of the excess that would be determined under this subparagraph if this subparagraph were read without reference to this clause that represents a payment to which

paragraph (*g*) or (*h*) of the definition "disposition" in subsection 248(1) applies, and

(iii) all amounts each of which is an eligible offset at that time of the taxpayer in respect of the former interest; and

(*d*) notwithstanding paragraphs (*a*) to (*c*), where the trust is non-resident at that time and the property is not described in paragraph (2.001)(*b*) or (*c*),

(i) the trust is deemed to have disposed of the property for proceeds equal to the cost amount of the property,

(ii) the beneficiary is deemed to have acquired the property at a cost equal to the fair market value of the property, and

(iii) the beneficiary's proceeds of disposition of the portion of the former interest disposed of by the beneficiary on the distribution are deemed to be equal to the fair market value of the property.

Gains not flowed-out to beneficiaries

(2.11) Where a trust makes one or more distributions of property in a taxation year in circumstances to which subsection (2.1) applies (or, in the case of property distributed after October 1, 1996 and before 2000, in circumstances to which subsection (5) applied)

(*a*) where the trust is resident in Canada at the time of each of those distributions and has so elected in prescribed form filed with the trust's return for the year or a preceding taxation year, the income of the trust for the year (determined without reference to subsection 104(6)) shall, for the purposes of subsections 104(6) and (13), be computed without regard to all of those distributions to non-resident persons (including a partnership other than a Canadian partnership); and

(*b*) where the trust is resident in Canada at the time of each of those distributions and has so elected in prescribed form filed with the trust's return for the year or a preceding taxation year, the income of the trust for the year (determined without reference to subsection 104(6)) shall, for the purposes of subsections 104(6) and (13), be computed without regard to all of those distributions.

(12) Subsection 107(3) of the Act is repealed.

(13) Subsection 107(4) of the Act is replaced by the following:

Trusts in favour of spouse or self

(4) Subsection (2.1) applies at any time to property distributed to a beneficiary by a trust described in paragraph 104(4)(*a*) where

(*a*) the beneficiary is not

(i) in the case of a post-1971 spousal trust, the spouse referred to in paragraph 104(4)(*a*),

(ii) in the case of an *alter ego* trust, the taxpayer referred to in paragraph 104(4)(*a*), and

(iii) in the case of a joint spousal trust, the taxpayer or the spouse referred to in paragraph 104(4)(*a*); and

(*b*) a taxpayer or spouse referred to in subparagraph (*a*)(i), (ii), or (iii), as the case may be, is alive on the day of the distribution.

(14) The portion of subsection 107(4.1) of the Act after paragraph (*c*) is replaced by the following:

subsection (2.1) applies in respect of the distribution.

(15) Subsection 107(5) of the Act is replaced by the following:

Distribution to non-resident

(5) Subsection (2.1) applies in respect of a distribution of a property (other than a share of the capital stock of a non-resident-owned investment corporation or property described in any of subparagraphs 128.1(4)(*b*)(i) to (iii)) by a trust resident in Canada to a non-resident taxpayer (including a partnership other than a Canadian partnership) in satisfaction of all or part of the taxpayer's capital interest in the trust.

Instalment interest

(5.1) Where, solely because of the application of subsection (5), paragraphs (2)(*a*) to (*c*) do not apply to a distribution in a taxation year of taxable Canadian property by a trust, in applying sections 155, 156 and 156.1 and subsections 161(2), (4) and (4.01) and any regulations made for the purpose of those provisions, the trust's total taxes payable under this Part and Part I.1 for the year are deemed to be the lesser of

(*a*) the trust's total taxes payable under this Part and Part I.1 for the year, determined before taking into consideration the specified future tax consequences for the year, and

(*b*) the amount that would be determined under paragraph (*a*) if subsection (5) did not apply to each distribution in the year of taxable Canadian property to which the rules in subsection (2) do not apply solely because of the application of subsection (5).

(16) Subsections (1) to (4) apply to the 2000 and subsequent taxation years.

(17) Subsection (5) applies to distributions made after October 1, 1996.

(18) Subsections (6) and (7), subsection 107(2.002) of the Act, as enacted by subsection (9), and subsections (10) and (12) to (14) apply to distributions made after 1999, except that for distributions made to a beneficiary before the particular day on which this Act is assented to, an election under subsection 107(2.002), as enacted by subsection (9), is deemed to have been made in a timely manner if it is made on or before the beneficiary's filing-due date for the taxation year that includes the particular day.

(19) Subsection (8) applies in determining after October 1, 1996 whether property is taxable Canadian property.

(20) Subsection 107(2.001) of the Act, as enacted by subsection (9), applies to distributions made after October 1, 1996, except that for distributions made from a trust before the particular day on which this Act is assented to, an election under subsection 107(2.001) of the Act, as enacted by subsection (9), is deemed to have been made in a timely manner if it is made on or before the trust's filing-due date for the taxation year that includes the particular day.

(21) Subsection 107(2.1) of the Act, as enacted by subsection (11), applies to distributions made after 1999 (other than distributions made before March 2000 in satisfaction of rights described in subsection 52(6) of the Act that were acquired before 2000).

(22) Subsection 107(2.11) of the Act, as enacted by subsection (11), applies to distributions made after October 1, 1996, except that for distributions made from a trust before the particular day on which this Act is assented to, an election under subsection 107(2.11) of the Act, as enacted by subsection (11), is deemed to have been made in a timely manner if it is made on or

before the trust's filing-due date for the taxation year that includes the particular day.

(23) Subsection (15) applies to distributions made after October 1, 1996, except that for distributions made after October 1, 1996 and before 2000, subsection 107(5) of the Act, as enacted by subsection (15), shall be read as follows:

(5) Where subsection (2) applies to a distribution at any time by a trust resident in Canada of a property (other than a share of the capital stock of a non-resident-owned investment corporation or property described in any of subparagraphs 128.1(4)(*b*)(i) to (iii)) to a non-resident taxpayer (including a partnership other than a Canadian partnership) who is a beneficiary under the trust in satisfaction of the taxpayer's capital interest in the trust, notwithstanding paragraphs (2)(*a*) to (*c*),

(*a*) the trust is deemed to have disposed of the property for proceeds equal to its fair market value at that time;

(*b*) the taxpayer is deemed to have acquired the property at a cost equal to that fair market value; and

(*c*) the taxpayer is deemed to have disposed of all or part, as the case may be, of the taxpayer's capital interest in the trust, for proceeds of disposition equal to the adjusted cost base to the taxpayer of that interest or part of the interest, as the case may be, immediately before that time.

18. (1) The Act is amended by adding the following after section 107.3:

Qualifying disposition

107.4 (1) For the purpose of this section, a "qualifying disposition" of a property means a disposition of the property by a person or partnership (in this subsection referred to as the "contributor") as a result of a transfer of the property to a particular trust where

(*a*) because of the disposition, there is a change in the legal ownership of the property that does not result in a change in the beneficial ownership of the property;

(*b*) the proceeds of disposition would, if this Act were read without reference to this section and sections 69 and 73, not be determined under any provision of this Act;

(*c*) if the particular trust is non-resident, the disposition is not

(i) by a person resident in Canada or by a partnership (other than a partnership each member of which is non-resident), or

(ii) a transfer of taxable Canadian property from a non-resident person who was resident in Canada in any of the ten calendar years preceding the transfer;

(*d*) the contributor is not a partnership, if the disposition is part of a series of transactions or events that begin after **ANNOUNCEMENT DATE** that includes the cessation of the partnership's existence and a subsequent distribution from a personal trust to a former member of the partnership in circumstances to which subsection 107(2) applies;

(*e*) unless the contributor is a trust, there is immediately after the disposition no absolute or contingent right of a person or partnership (other than the contributor or, where the property was jointly owned, each of the joint contributors) as a beneficiary (determined with reference to subsection 104(1.1)) under the particular trust;

(*f*) the contributor is not an individual (other than a trust described in any of paragraphs (*a*) to (*e*.1) of the definition "trust" in subsection 108(1)), if the particular trust is described in any of paragraphs (*a*) to (*e*.1) of the definition "trust" in subsection 108(1);

(*g*) the disposition is not part of a series of transactions or events that begins after **ANNOUNCEMENT DATE** and that includes

(i) the subsequent acquisition, for consideration given to a personal trust, of a capital interest or an income interest in the trust,

(ii) the disposition of all or part of a capital interest or an income interest in a personal trust, other than a disposition solely as a consequence of a distribution from a trust to a person or partnership in satisfaction of all or part of that interest, or

(iii) the transfer to a trust of property as consideration for the acquisition of a capital interest in another trust, if that property can reasonably be considered to have been received in order to fund distributions from the other trust (other than distributions representing proceeds of disposition of capital interests in the other trust);

(*h*) the disposition is not, and is not part of, a transaction that occurs after **ANNOUNCEMENT DATE** and that includes the giving to the

contributor, for the disposition, of any consideration (other than consideration that is an interest of the contributor as a beneficiary under the particular trust or that is the assumption by the particular trust of debt for which the property may, at the time of the disposition, reasonably be considered to be security);

(*i*) subsection 73(1) does not apply to the disposition and would not apply to the disposition if

(i) no election had been made under that subsection, and

(ii) section 73 were read without reference to subsection 73(1.02); and

(*j*) if the contributor is an amateur athlete trust, a cemetery care trust, an employee trust, an *inter vivos* trust deemed by subsection 143(1) to exist in respect of a congregation that is a constituent part of a religious organization, a related segregated fund trust (as defined by section 138.1), a trust described in paragraph 149(1)(*o*.4) or a trust governed by an eligible funeral arrangement, an employees profit sharing plan, a registered education savings plan or a registered supplementary unemployment benefit plan, the particular trust is the same type of trust.

Division of trust property among other trusts

(2) For the purpose of paragraph (1)(*a*), where a trust (in this subsection referred to as the "transferor trust"), in a period that does not exceed one day, disposes of one or more properties in the period to one or more other trusts, any resulting change in the legal ownership of those properties is deemed not to result in a change in the beneficial ownership of those properties if

(*a*) the transferor trust receives no consideration for the disposition; and

(*b*) as a consequence of the disposition, the beneficial ownership at the beginning of the period of each beneficiary under the transferor trust in each particular property of the transferor trust is the same as the beneficiary's beneficial ownership at the end of the period in the particular property that relates to the beneficiary's combined interest in the transferor trust and in the other trust or trusts.

Tax consequences of qualifying dispositions

(3) Where at a particular time there is a qualifying disposition of a property by a person or partnership (in this subsection referred to as the "transferor") to a trust (in this subsection referred to as the "transferee trust"),

(*a*) the transferor's proceeds of disposition of the property are deemed to be

(i) where the transferor so elects in writing on or before the transferor's filing-due date for its taxation year that includes the particular time, or at such later time as is acceptable to the Minister, the amount specified in the election that is not less than the cost amount to the transferor of the property immediately before the particular time and not more than the fair market value of the property at the particular time, and

(ii) in any other case, the cost amount to the transferor of the property immediately before the particular time;

(*b*) except as otherwise provided under paragraph (*c*), the transferee trust's cost of the property is deemed to be the amount, if any, by which

(i) the proceeds determined under paragraph (*a*) in respect of the qualifying disposition,

exceed

(ii) the amount by which the transferor's loss otherwise determined from the qualifying disposition would be reduced because of subsection 100(4), paragraph 107(1)(*c*) or (*d*) or any of subsections 112(3) to (4.2), if the proceeds determined under paragraph (*a*) were equal to the fair market value of the property at the particular time;

(*c*) notwithstanding subsection 206(4), for the purposes of Part XI and regulations made for the purposes of Part XI, the transferee trust's cost of the property is deemed to be

(i) where the transferee trust so elects in writing on or before its filing due-date for its taxation year that includes the particular time and it may reasonably be considered that the election was not made for the purpose of avoiding tax under Part XI, the fair market value of the property at the particular time, and

(ii) in any other case, the cost amount to the transferor of the property immediately before the particular time;

(*d*) if the property was depreciable property of a prescribed class of the transferor and its capital cost to the transferor exceeds the cost at which the transferee trust is deemed by this subsection to have acquired the property, for the purposes of sections 13 and 20 and any regulations made for the purpose of paragraph 20(1)(*a*),

(i) the capital cost of the property to the transferee trust is deemed to be the amount that was the capital cost of the property to the transferor, and

(ii) the excess is deemed to have been allowed to the transferee trust in respect of the property under regulations made for the purpose of paragraph 20(1)(*a*) in computing income for taxation years that ended before the particular time;

(*e*) if the property was eligible capital property of the transferor in respect of a business of the transferor,

(i) where the eligible capital expenditure of the transferor in respect of the property exceeds the cost at which the transferee trust is deemed by this subsection to have acquired the property, for the purposes of sections 14, 20 and 24,

(A) the eligible capital expenditure of the transferee trust in respect of the property is deemed to be the amount that was the eligible capital expenditure of the transferor in respect of the property, and

(B) 3/4 of the excess is deemed to have been allowed under paragraph 20(1)(*b*) to the transferee trust in respect of the property in computing income for taxation years that ended

(I) before the particular time, and

(II) after the adjustment time of the transferee trust in respect of the business, and

(ii) for the purpose of determining after the particular time the amount to be included under subparagraph 14(1)(*a*)(v) or paragraph 14(1)(*b*) in computing the transferee trust's income in respect of any subsequent disposition of the property of the business, there shall be added to the value otherwise determined

for Q in the definition "cumulative eligible capital" in subsection 14(5) the amount determined by the formula

A x B/C

where

A is the amount, if any, determined for Q in that definition in respect of the business of the transferor immediately before the particular time,

B is the fair market value of the property immediately before the particular time, and

C is the fair market value immediately before the particular time of all eligible capital property of the transferor in respect of the business;

(*f*) if the property was deemed to be taxable Canadian property of the transferor by this paragraph or paragraph 51(1)(*f*), 85(1)(*i*) or 85.1(1)(*a*), subsection 87(4) or (5) or paragraph 97(2)(*c*) or 107(2)(*d*.1), the property is deemed to be taxable Canadian property of the transferee trust;

(*g*) where the transferor is a related segregated fund trust (in this paragraph having the meaning assigned by section 138.1),

(i) paragraph 138.1(1)(*i*) does not apply in respect of a disposition of an interest in the transferor that occurs in connection with the qualifying disposition, and

(ii) in computing the amount determined under paragraph 138.1(1)(*i*) in respect of a subsequent disposition of an interest in the transferee trust where the interest is deemed to exist in connection with a particular life insurance policy, the acquisition fee (as defined by subsection 138.1(6)) in respect of the particular policy shall be determined as if each amount determined under any of paragraphs 138.1(6)(*a*) to (*d*) in respect of the policyholder's interest in the transferor trust had been determined in respect of the policyholder's interest in the transferee trust;

(*h*) if the transferor is a trust to which property had been transferred by an individual (other than a trust),

(i) where subsection 73(1) applied in respect of the property so transferred and it is reasonable to consider that the property was so transferred in anticipation of the individual ceasing to be

resident in Canada, for the purposes of paragraph 104(4)(*a*.3) and the application of this paragraph to a disposition by the transferee trust after the particular time, the transferee trust is deemed after the particular time to be a trust to which the individual had transferred property in anticipation of the individual ceasing to reside in Canada and in circumstances to which subsection 73(1) applied, and

(ii) for the purposes of paragraph (*j*) of the definition "excluded personal property" in subsection 128.1(9) and the application of this paragraph to a disposition by the transferee trust after the particular time, where the property so transferred was transferred in circumstances to which this subsection would apply if subsection (1) were read without reference to paragraphs (1)(*h*) and (*i*), the transferee trust is deemed after the particular time to be a trust an interest in which was acquired by the individual as a consequence of a qualifying disposition;

(*i*) if the transferor is a trust (other than a personal trust or a trust prescribed for the purposes of subsection 107(2)), the transferee trust is deemed to be neither a personal trust nor a trust prescribed for the purposes of subsection 107(2);

(*j*) if the transferor is a trust and a taxpayer disposes of all or part of a capital interest in the transferor because of the qualifying disposition and, as a consequence, acquires a capital interest or part of it in the transferee trust

(i) the taxpayer is deemed to dispose of the capital interest or part of it in the transferor for proceeds equal to the cost amount to the taxpayer of that interest or part of it immediately before the particular time, and

(ii) the taxpayer is deemed to acquire the capital interest or part thereof in the transferee trust at a cost equal to the amount, if any, by which

(A) that cost amount

exceeds

(B) the amount by which the taxpayer's loss otherwise determined from the disposition referred to in subparagraph (i) would be reduced because of paragraph 107(1)(*c*) or (*d*) if the proceeds under that subparagraph were equal to the fair market value of the capital interest or part of it in the transferor immediately before the particular time;

(*k*) where the transferor is a trust, a taxpayer's beneficial ownership in the property ceases to be derived from the taxpayer's capital interest in the transferor because of the qualifying disposition and no part of the taxpayer's capital interest in the transferor was disposed of because of the qualifying disposition, there shall, immediately after the particular time, be added to the cost otherwise determined of the taxpayer's capital interest in the transferee trust, the amount determined by the formula

$$A \times ((B-C)/B) - D$$

where

A is the cost amount to the taxpayer of the taxpayer's capital interest in the transferor immediately before the particular time,

B is the fair market value immediately before the particular time of the taxpayer's capital interest in the transferor,

C is the fair market value at the particular time of the taxpayer's capital interest in the transferor (determined as if the only property disposed of at the particular time were the particular property), and

D is the lesser of

(i) the amount, if any, by which the cost amount to the taxpayer of the taxpayer's capital interest in the transferor immediately before the particular time exceeds the fair market value of the taxpayer capital interest in the transferor immediately before the particular time, and

(ii) the maximum amount by which the taxpayer's loss from a disposition of a capital interest otherwise determined could have been reduced because of paragraph 107(1)(*c*) or (*d*) if the taxpayer's capital interest in the transferor had been disposed of immediately before the particular time;

(*l*) where paragraph (*k*) applies to the qualifying disposition in respect of a taxpayer, the amount that would be determined under paragraph (*k*) in respect of the qualifying disposition if the amount determined for D in that paragraph were nil shall, immediately after the particular time, be deducted in computing the cost otherwise determined of the taxpayer's capital interest in the transferor;

(*m*) where paragraphs (*j*) and (*k*) do not apply in respect of the qualifying disposition, the transferor is deemed to acquire the capital

interest or part thereof in the transferee trust that is acquired as a consequence of the qualifying disposition

(i) where the transferee trust is a personal trust, at a cost equal to nil, and

(ii) in any other case, at a cost equal to the excess determined under paragraph (*b*) in respect of the qualifying disposition; and

(*n*) if the transferor is a trust and a taxpayer disposes of all or part of an income interest in the transferor because of the qualifying disposition and, as a consequence, acquires an income interest or a part of an income interest in the transferee trust, for the purpose of subsection 106(2), the taxpayer is deemed not to dispose any part of the income interest in the transferor at the particular time.

Fair market value of vested interest in trust

(4) Where

(*a*) a particular capital interest in a trust is held by a beneficiary at any time,

(*b*) the particular interest is vested indefeasibly at that time,

(*c*) the trust is not described in any of paragraphs (*a*) to (*e*.1) of the definition "trust" in subsection 108(1), and

(*d*) interests under the trust are not ordinarily disposed of for consideration that reflects the fair market value of the net assets of the trust,

the fair market value of the particular interest at that time is deemed to be not less than the amount determined by the formula

$$(A - B) \times (C/D)$$

where

A is the total fair market value at that time of all properties of the trust,

B is the total of all amounts each of which is the amount of a debt owing by the trust at that time or the amount of any other obligation of the trust to pay any amount that is outstanding at that time,

C is the fair market value at that time of the particular interest (determined without reference to this subsection), and

D is the total fair market value at that time of all interests as beneficiaries under the trust (determined without reference to this subsection).

(2) Subsections 107.4(1) and (3) of the Act, as enacted by subsection (1), apply

(*a*) to dispositions that occur after December 23, 1998, and

(*b*) for the purpose of applying those subsections to the 1993 and subsequent taxation years, to transfers of capital property that occurred before December 24, 1998, except that, in its application to transfers before December 24, 1998,

(i) subsection 107.4(1) of the Act, as enacted by subsection (1), shall be read as follows:

107.4 (1) For the purpose of this section, a "qualifying disposition" of a property means a transfer of the property to a particular trust that was not a disposition of the property for the purpose of subdivision c because of paragraph (*e*) of the definition "disposition" in section 54, except where

(*a*) if the transfer is from another trust to the particular trust,

(i) each trust can reasonably be considered to act as agent for the same beneficiary or beneficiaries in respect of the property transferred, or

(ii) the transferee trust can reasonably be considered to act as agent for the transferor trust in respect of the property transferred; and

(*b*) in any other case, it is reasonable to consider that the particular trust acts as agent in respect of the property transferred.

(ii) the portion of subsection 107.4(3) of the Act before paragraph (*a*), as enacted by subsection (1), shall be read as follows:

(3) Where at a particular time there is a qualifying disposition of a property by a person or partnership (in this subsection referred to as the "transferor") to a trust (in this subsection

referred to as the "transferee trust"), except for the purposes of Part XI and regulations made for the purposes of Part XI

(iii) subsection 107.4(3) of the Act, as enacted by subsection (1), shall be read without reference to paragraphs 107.4(3)(*a*), (*c*), (*g*) and (*h*) of the Act, as enacted by subsection (1);

(iv) paragraph 107.4(3)(*b*) of the Act, as enacted by subsection (1), shall be read as follows:

(*b*) the transferee trust's cost of the property is deemed to be the cost amount to the transferor of the property immediately before the particular time;

(v) subsection 107.4(3) of the Act, as enacted by subsection (1), shall be read as if each amount determined under clause 107.4(3)(*j*)(ii)(B) of the Act and the description of D in paragraph 107.4(3)(*k*) of the Act, as enacted by subsection (1), were nil; and

(vi) subparagraph 107.4(3)(*m*)(ii) of the Act, as enacted by subsection (1), shall be read as follows:

(ii) in any other case, at a cost equal to the amount determined under paragraph (*b*) in respect of the qualifying disposition.

(3) Subsections 107.4(2) and (4) of the Act, as enacted by subsection (1), apply to dispositions that occur after December 23, 1998.

19. (1) The definition "accumulating income" in subsection 108(1) of the Act is replaced by the following:

"accumulating income"
« revenu accumulé »

"accumulating income" of a trust for a taxation year means the amount that would be the income of the trust for the year if that amount were computed

(*a*) without reference to paragraphs 104(4)(*a*) and (*a*.1) and subsections 104(5.1), (5.2) and (12) and 107(4),

(*b*) as if the greatest amount that the trust was entitled to claim under subsection 104(6) in computing its income for the year were so claimed, and

(*c*) without reference to subsection 12(10.2), except to the extent that that subsection applies to amounts paid to a trust to which paragraph 70(6.1)(*b*) applies and before the death of the spouse referred to in that paragraph;

(2) The definition "capital interest" in subsection 108(1) of the Act is replaced by the following:

"capital interest"
« participation au capital »

"capital interest" of a taxpayer in a trust means all rights of the taxpayer as a beneficiary under the trust, and after 1999 includes a right (other than a right acquired before 2000 and disposed of before March 2000) to enforce payment by the trust that arises as a consequence of any such right, but does not include an income interest in the trust;

(3) The portion of the definition "cost amount" in subsection 108(1) of the Act before paragraph (*a*) is replaced by the following:

"cost amount"
« coût indiqué »

"cost amount" to a taxpayer at any time of a capital interest or part of the interest, as the case may be, in a trust (other than a trust that is a foreign affiliate of the taxpayer) means, except for the purposes of section 107.4 and notwithstanding subsection 248(1),

(4) The definition "cost amount" in subsection 108(1) of the Act is amended by striking out the word "and" at the end of paragraph (*a*) and by adding the following after paragraph (*a*):

(*a*.1) where that time is immediately before the time of the death of the taxpayer and subsection 104(4) or (5) deems the trust to dispose of property at the end of the day that includes that time, the amount that would be determined under paragraph (*b*) if the taxpayer had died on a day that ended immediately before that time, and

(5) The definition "income interest" in subsection 108(1) of the Act is replaced by the following:

"income interest"
« participation
au revenu »

"income interest" of a taxpayer in a trust means a right (whether immediate or future and whether absolute or contingent) of the taxpayer as a beneficiary under a personal trust to, or to receive, all or any part of the income of the trust and, after 1999, includes a right (other than a right acquired before 2000 and disposed of before March 2000) to enforce payment by the trust that arises as a consequence of any such right;

(6) The portion of the definition "trust" in subsection 108(1) of the Act after paragraph (*e*.1) is replaced by the following:

and, in applying subsections 104(4), (5), (5.2), (12), (14) and (15) and section 106 at any time, does not include

(*f*) a trust that, at that time, is a unit trust, or

(*g*) a trust all interests in which, at that time, have vested indefeasibly, other than

(i) an *alter ego* trust, a joint spousal trust or a post-1971 spousal trust,

(ii) a trust that has elected under subsection 104(5.3),

(iii) a trust that has, in its return of income under this Part for its first taxation year ending after 1992, elected that this paragraph not apply,

(iv) a trust that is at that time resident in Canada where the total fair market value at that time of all interests in the trust held at that time by beneficiaries under the trust who at that time are non-resident is more than 20% of the total fair market value at that time of all interests in the trust held at that time by beneficiaries under the trust,

(v) a trust under the terms of which all or part of a person's interest in the trust is terminated with reference to a period of time (including a period of time determined with reference to the person's death), otherwise than as a consequence of terms of the trust under which an interest in the trust is to be terminated as a consequence of a distribution to the person (or the person's estate) of property of the trust if the fair market value of the property to be distributed is required to be commensurate with the

fair market value of that interest immediately before the distribution, or

(vi) a trust that, before that time and after **ANNOUNCEMENT DATE**, has made a distribution to a beneficiary in respect of the beneficiary's capital interest in the trust, if the distribution may reasonably be considered to have been financed by a liability of the trust and one of the purposes of incurring the liability was to avoid taxes otherwise payable under this Part as a consequence of the death of any individual;

(7) Subsection 108(1) of the Act is amended by adding the following in alphabetical order:

"eligible offset"
« montant de réduction admissible »

"eligible offset" at any time of a taxpayer in respect of all or part of the taxpayer's capital interest in a trust is the portion of any debt or obligation that is assumed by the taxpayer and that can reasonably be considered to be applicable to property distributed at that time in satisfaction of the interest or part of the interest, as the case may be, if the distribution is conditional upon the assumption by the taxpayer of the portion of the debt or obligation;

"exempt property"
« bien exonéré »

"exempt property" of a taxpayer at any time means property any income or gain from the disposition of which by the taxpayer at that time would, because the taxpayer is non-resident or because of a provision contained in a tax treaty, not cause an increase in the taxpayer's tax payable under this Part;

(8) Paragraph 108(2)(*b*) of the Act is replaced by the following:

(*b*) each of the following conditions was satisfied:

(i) throughout the taxation year that includes the particular time (in this paragraph referred to as the "current year"), the trust was resident in Canada,

(ii) throughout the period or periods (in this paragraph referred to as the "relevant periods") that are in the current year and throughout which the conditions in paragraph (*a*) are not satisfied in respect of the trust, its only undertaking was

(A) the investing of its funds in property (other than real property or an interest in real property),

(B) the acquiring, holding, maintaining, improving, leasing or managing of any real property, or interest in real property, that is capital property of the trust, or

(C) any combination of the activities described in clauses (A) and (B),

(iii) throughout the relevant periods at least 80% of its property consisted of any combination of

(A) shares,

(B) any property that, under the terms or conditions of which or under an agreement, is convertible into, is exchangeable for or confers a right to acquire, shares,

(C) cash,

(D) bonds, debentures, mortgages, notes and other similar obligations,

(E) marketable securities,

(F) real property situated in Canada and interests in real property situated in Canada, and

(G) rights to and interests in any rental or royalty computed by reference to the amount or value of production from a natural accumulation of petroleum or natural gas in Canada, from an oil or gas well in Canada or from a mineral resource in Canada,

(iv) either

(A) not less than 95% of its income for the current year (computed without regard to subsections 49(2.1) and 104(6)) was derived from, or from the disposition of, investments described in subparagraph (iii), or

(B) not less than 95% of its income for each of the relevant periods (computed without regard to subsections 49(2.1) and 104(6) and as though each of those periods were a taxation year) was derived from, or from the disposition of, investments described in subparagraph (iii),

(v) throughout the relevant periods, not more than 10% of its property consisted of bonds, securities or shares in the capital stock of any one corporation or debtor other than Her Majesty in right of Canada or a province or a Canadian municipality, and

(vi) where the trust would not be a unit trust at the particular time if this paragraph were read without reference to this subparagraph and subparagraph (iii) were read without reference to clause (F), the units of the trust are listed at any time in the current year or in the following taxation year on a prescribed stock exchange in Canada, or

(9) The portion of subsection 108(3) of the Act before paragraph (*a*) is replaced by the following:

Income of a trust in certain provisions

(3) For the purposes of the definition "income interest" in subsection (1), the income of a trust is its income computed without reference to the provisions of this Act and, for the purposes of the definition "pre-1972 spousal trust" in subsection (1) and paragraphs 70(6)(*b*) and (6.1)(*b*), 73(1.01)(*c*) and 104(4)(*a*), the income of a trust is its income computed without reference to the provisions of this Act, minus any dividends included in that income

(10) Subsection 108(4) of the Act is replaced by the following:

Trust not disqualified

(4) For the purposes of the definition "pre-1972 spousal trust" in subsection (1), subparagraphs 70(6)(*b*)(ii) and (6.1)(*b*)(ii) and paragraphs 73(1.01)(*c*) and 104(4)(*a*), where a trust was created by a taxpayer whether by the taxpayer's will or otherwise, no person is deemed to have received or otherwise obtained or to be entitled to receive or otherwise obtain the use of any income or capital of the trust solely because of the payment, or provision for payment, as the case may be, by the trust of

(*a*) any estate, legacy, succession or inheritance duty payable, in consequence of the death of the taxpayer or a spouse of the taxpayer who is a beneficiary under the trust, in respect of any property of, or interest in, the trust; or

(*b*) any income or profits tax payable by the trust in respect of any income of the trust.

(11) Subsection 108(6) of the Act is replaced by the following:

Variation of trusts

(6) Where at any time the terms of a trust are varied

(*a*) for the purposes of subsections 104(4), (5) and (5.2), subject to paragraph (*b*), the trust is, at and after that time, deemed to be the same trust as, and a continuation of, the trust immediately before that time;

(*b*) for greater certainty, paragraph (*a*) does not affect the application of paragraph 104(4)(*a*.1); and

(*c*) for the purposes of paragraph 53(2)(*h*), subsection 107(1), paragraph (*j*) of the definition "excluded personal property" in subsection 128.1(9) and the definition "personal trust" in subsection 248(1), no interest of a beneficiary under the trust before it was varied is considered to be consideration for the interest of the beneficiary in the trust as varied.

Interests acquired for consideration

(7) For the purposes of paragraph 53(2)(*h*), subsection 107(1), paragraph (*j*) of the definition "excluded personal property" in subsection 128.1(9) and the definition "personal trust" in subsection 248(1),

(*a*) an interest in a trust is deemed not to be acquired for consideration solely because it was acquired in satisfaction of any right as a beneficiary under the trust to enforce payment from the trust; and

(*b*) where all the beneficial interests in a particular *inter vivos* trust acquired by way of the transfer, assignment or other disposition of property to the particular trust were acquired by

(i) one person, or

(ii) two or more persons who would be related to each other if

(A) a trust and another person were related to each other, where the other person is a beneficiary under the trust or is related to a beneficiary under the trust, and

(B) a trust and another trust were related to each other, where a beneficiary under the trust is a beneficiary under the other trust or is related to a beneficiary under the other trust,

any beneficial interest in the particular trust acquired by such a person is deemed to have been acquired for no consideration.

(12) Subsection (1) and subsection 108(6) of the Act, as enacted by subsection (11), apply to the 2000 and subsequent taxation years.

(13) Subsection (2) applies after 1999.

(14) Subsection (3) applies to the 1993 and subsequent taxation years.

(15) Subsection (4) applies to deaths that occur after 1999.

(16) Subsection (5) applies in respect of interests created or materially altered after January 31, 1987 that were acquired after 10 p.m. EST, February 6, 1987.

(17) Subsection (6) applies to the 1998 and subsequent taxation years, except that

(*a*) it does not apply for the purpose of applying subparagraph (*g*)(iv) of the definition "trust" in subsection 108(1) of the Act, as enacted by subsection (6), on or before December 23, 1998; and

(*b*) where the trust so elects in writing on or before the trust's filing-due date for taxation year of the trust that includes the date on which this Act is assented to (or such later day as is acceptable to the Minister), subparagraph (*g*)(v) of that definition, as it applies before 2001, shall be read as follows:

(v) a trust any interest in which may become effective in the future, or

(18) The definition "eligible offset" in subsection 108(1) of the Act, as enacted by subsection (7), applies after 1999.

(19) The definition "exempt property" in subsection 108(1) of the Act, as enacted by subsection (7), applies after 1992, except that before 1999, the words "tax treaty" in that definition shall be read as "convention or agreement with another country that has the force of law in Canada".

(20) Subsection (8) applies to the 1998 and subsequent taxation years.

(21) Subsections (9) and (10) apply to the 2000 and subsequent taxation years, except for the purpose of applying section 73 of the Act to transfers that occur before 2000.

(22) Subsection 108(7) of the Act, as enacted by subsection (11), apply after December 23, 1998.

20. (1) The portion of subsection 110.6(12) of the Act before paragraph (*a*) is replaced by the following:

Spousal trust deduction

(12) Notwithstanding any other provision of this Act, a trust described in paragraph 104(4)(*a*) or (*a*.1) (other than a trust that elected under subsection 104(5.3), an *alter ego* trust or a joint spousal trust) may, in computing its taxable income for its taxation year that includes the day determined under paragraph 104(4)(*a*) or (*a*.1), as the case may be, in respect of the trust, deduct under this section an amount equal to the least of

(2) Subsection (1) applies to 2000 and subsequent taxation years.

21. (1) Subsection 122(2) of the Act is amended by striking out the word "and" at the end of paragraph (*d*), by adding the word "and" at the end of paragraph (*e*) and by adding the following after paragraph (*e*):

(*f*) has not received any property after **ANNOUNCEMENT DATE** because of a transfer from another trust, where

(i) subsection (1) was applicable to a taxation year of the other trust that began before the property was so received, and

(ii) because of the transfer, there is a change in the legal ownership of the property that does not result in a change in the beneficial ownership of the property.

(2) Subsection (1) applies to 1999 and subsequent taxation years.

22. (1) Section 132 of the Act is amended by adding the following after subsection (6.1):

Retention of status as mutual fund trust

(6.2) Except for the purposes of this subsection, a trust is deemed to be a mutual fund trust throughout a calendar year where

(*a*) at any time in the year, the trust ceased to be a mutual fund trust because of the application of paragraph 132(6)(*c*);

(*b*) the trust was, at the beginning of the year, a mutual fund trust; and

(*c*) the trust would, throughout the portion of the year throughout which it was in existence, have been a mutual fund trust if subsection 132(6) were read without reference to paragraph (*c*) of that subsection.

(2) Paragraphs 132(7)(*a*) and (*b*) of the Act are replaced by the following:

(*a*) throughout the period that began on the later of February 21, 1990 and the day of its creation and ended at that time, all or substantially all of its property consisted of property other than property that would be taxable Canadian property if the definition "taxable Canadian property" in subsection 248(1) were read without reference to paragraph (*b*) of that definition; or

(*b*) it has not issued any unit (other than a unit issued to a person as a payment, or in satisfaction of the person's right to enforce payment, out of the trust's income, determined before the application of subsection 104(6) or out of the trust's capital gains) of the trust after February 20, 1990 and before that time to a person who, after reasonable inquiry, it had reason to believe was non-resident, except where the unit was issued to that person under an agreement in writing entered into before February 21, 1990.

(3) Subsection (1) applies to the 1990 and subsequent taxation years.

(4) Paragraph 132(7)(*a*) of the Act, as enacted by subsection (2), applies after October 1, 1996.

(5) Paragraph 132(7)(*b*) of the Act, as enacted by subsection (2), applies after February 20, 1990.

23. (1) Subsection 132.11(4) of the Act is replaced by the following:

Amounts paid or payable to beneficiaries

(4) For the purposes of subsections (5) and (6) and subsections 104(6) and (13), notwithstanding subsection 104(24), each amount that is paid, or that becomes payable, by a trust to a beneficiary after the end of a particular taxation year of the trust that ends on December 15 of a calendar year because of subsection (1) and before the end of that calendar year, is deemed to have been paid or to have become payable, as the case may be, to the beneficiary at the end of the particular year and not at any other time.

(2) Subsection 132.11(6) of the Act is amended by adding the word "and" at the end of paragraph (*a*), by striking out the word "and" at the end of paragraph (*b*) and by repealing paragraph (*c*).

(3) Subsections (1) and (2) apply to the 2000 and subsequent taxation years.

24. (1) Subsection 159(6.1) of the Act is replaced by the following:

Election where subsection 104(4) applicable

(6.1) Where a day determined under paragraph 104(4)(*a*), (*a*.1), (*a*.2), (*a*.3), (*b*) or (*c*) in respect of a trust occurs in a taxation year of the trust and the trust so elects and furnishes to the Minister security acceptable to the Minister for payment of any tax the payment of which is deferred by the election, notwithstanding any other provision of this Part respecting the time within which payment shall be made of the tax payable under this Part by the trust for the year, all or any portion of such part of that tax as is equal to the amount, if any, by which that tax exceeds the amount that that tax would be if this Act were read without reference to paragraph 104(4)(*a*), (*a*.1), (*a*.2), (*a*.3), (*b*) or (*c*), as the case may be, may be paid in such number (not exceeding 10) of equal consecutive annual instalments as is specified by the trust in the election, the first instalment of which shall be paid on or before the day on or before which payment of that tax would, but for the election, have been required to be made and each subsequent instalment of which shall be paid on or before the next following anniversary of that day.

(2) Subsection (1) applies to 2000 and subsequent taxation years.

25. (1) Subsection 206(1) of the Act is amended by adding the following in alphabetical order:

"cost amount"
« coût indiqué »

"cost amount" at any time of a taxpayer's capital interest in a trust that is foreign property is deemed to be the greater of

(*a*) the cost amount of the interest, determined without reference to this definition, and

(*b*) where that time is more than 60 days after the end of a taxation year of the trust and subparagraph 53(2)(*h*)(i.1) applies (or would apply if that subparagraph were read without reference to clauses (A) and (B) of that subparagraph) in respect of an amount that became payable, after 1999 and at or before the end of the year in respect of the interest, that has not been satisfied at or before that time by the issue of new units in the trust, the amount that would be the cost amount at that time of the interest if new units of the trust had in every case been issued in satisfaction of each such amount payable;

(2) Subsection (1) applies after 2000.

26. (1) Paragraph 210.2(2)(*b*) of the Act is replaced by the following:

(*b*) the only taxable capital gains and allowable capital losses referred to in paragraph 3(*b*) were from dispositions of taxable Canadian property; and

(2) Subsection (1) applies after October 1, 1996.

27. (1) Subparagraph 212(1)(*c*)(i) of the Act is replaced by the following:

(i) is included in computing the income of the non-resident person under subsection 104(13), except to the extent that the amount is deemed by subsection 104(21) to be a taxable capital gain of the non-resident person, or

(2) Subsection (1) applies to amount paid or credited after ANNOUNCEMENT DATE.

28. (1) The portion of the definition "personal trust" in subsection 248(1) of the Act after subparagraph (*b*)(ii) is replaced by the following:

but, after 1999, does not include a unit trust;

(2) Subsection 248(1) of the Act is amended by adding the following in alphabetical order:

"*alter ego* trust"
« fiducie en faveur de soi-même »

"*alter ego* trust" means a trust to which paragraph 104(4)(*a*) would apply if that paragraph were read without reference to subparagraph 104(4)(*a*)(iii) and clause 104(4)(*a*)(iv)(B);

"disposition"
« disposition »

"disposition" of any property, except as expressly otherwise provided, includes

(*a*) any transaction or event entitling a taxpayer to proceeds of disposition of the property,

(*b*) any transaction or event by which,

(i) where the property is a share, bond, debenture, note, certificate, mortgage, agreement of sale or similar property, or an interest in it, the property is redeemed in whole or in part or is cancelled,

(ii) where the property is a debt or any other right to receive an amount, the debt or other right is settled or cancelled,

(iii) where the property is a share, the share is converted because of an amalgamation or merger, and

(iv) where the property is an option to acquire or dispose of property, the option expires,

(*c*) any transfer of the property to a trust or, where the property is property of a trust, any transfer of the property to any beneficiary under the trust, except as provided by paragraph (*f*), and

(*d*) where the property is, or is part of, a beneficiary's capital interest in a trust, except as provided by paragraphs (*g*) and (*h*), a payment made after 1999 to the beneficiary from the trust that can reasonably be considered to have been made because of the beneficiary's capital interest in the trust,

but does not include

(*e*) any transfer of the property as a consequence of which there is a change in the legal ownership of the property that does not result in any change in the beneficial ownership of the property, except where the transfer is

(i) from a person or a partnership to a trust for the benefit of the person or the partnership,

(ii) from a trust to a beneficiary under the trust in satisfaction of all or part of the beneficiary's interest in the trust, or

(iii) from one trust maintained for the benefit of one or more beneficiaries under the trust to another trust maintained for the benefit of the same beneficiaries,

(*f*) any transfer of the property as a consequence of which there is a change in the legal ownership of the property that does not result in any change in the beneficial ownership of the property, where

(i) the transferor and the transferee are trusts,

(ii) the transfer is not by a trust resident in Canada to a non-resident trust,

(iii) the transferee does not receive the property in satisfaction of the transferee's right as a beneficiary under the transferor trust,

(iv) the transferee held no property immediately before the transfer (other than property the cost of which is not included, for the purposes of this Act, in computing a balance of undeducted outlays, expenses or other amounts in respect of the transferee),

(v) neither the transferor nor the transferee make an election in writing filed with the Minister on or before the filing-due date for the taxation year of the transferor or transferee, as the case may be, in which the transfer is made (or on such later day as is acceptable to the Minister) that this paragraph not apply,

(vi) where the transferor is an amateur athlete trust, a cemetery care trust, an employee trust, an *inter vivos* trust deemed by subsection 143(1) to exist in respect of a congregation that is a constituent part of a religious organization, a related segregated fund trust (in this paragraph having the meaning assigned by section 138.1), a trust described in paragraph 149(1)(*o*.4) or a trust governed by an eligible funeral arrangement, an employees profit sharing plan, a registered education savings plan or a

registered supplementary unemployment benefit plan, the transferee is the same type of trust, and

(vii) the transfer results, or is part of a series of transactions that results, in the transferor ceasing to exist and, immediately before the time of the transfer or the beginning of that series of transactions, as the case may be, the transferee never held any property or held only property having a nominal value,

(*g*) where the property is part of a capital interest of a taxpayer in a trust (other than a personal trust or a trust prescribed for the purpose of subsection 107(2)) that is described by reference to units issued by the trust, a payment after 1999 from the trust in respect of the capital interest, where the number of units in the trust that are owned by the taxpayer is not reduced because of the payment,

(*h*) where the property is a capital interest in a trust, a payment after 1999 in respect of the capital interest to the extent that the payment

(i) is out of the income of the trust (determined without reference to subsection 104(6)) for a taxation year or out of the capital gains of the trust for the year, if the payment was made in the year or the right to the payment was acquired in the year, or

(ii) is in respect of an amount designated by the trust under subsection 104(20),

(*i*) any transfer of the property for the purpose only of securing a debt or a loan, or any transfer by a creditor for the purpose only of returning property that had been used as security for a debt or a loan,

(*j*) any transfer of the property to a trust as a consequence of which there is a change in the legal ownership of the property that does not result in any change in the beneficial ownership of the property, where the main purpose of the transfer is

(i) to provide for payment under a debt or loan,

(ii) to provide assurance that an absolute or contingent obligation of the transferor will be satisfied, or

(iii) to facilitate either the provision of compensation or the enforcement of a penalty, in the event that an absolute or contingent obligation of the transferor is not satisfied,

(*k*) any issue of a bond, debenture, note, certificate or mortgage, and

(*l*) any issue by a corporation of a share of its capital stock, or any other transaction that, but for this paragraph, would be a disposition by a corporation of a share of its capital stock;

"joint spousal trust"
« fiducie mixte au profit du conjoint »

"joint spousal trust" means a trust to which paragraph 104(4)(*a*) would apply if that paragraph were read without reference to subparagraph 104(4)(*a*)(iii) and clause 104(4)(*a*)(iv)(A);

"post-1971 spousal trust"
« fiducie au profit du conjoint postérieur à 1971 »

"post-1971 spousal trust" means a trust that would be described in paragraph 104(4)(*a*) if that paragraph were read without reference to subparagraph 104(4)(*a*)(iv);

(3) Section 248 of the Act is amended by adding the following after subsection (25):

Trust-to-trust transfers

(25.1) Where there is a transfer at a particular time of a property from a trust (in this subsection referred to as the "transferor") to another trust (in this subsection referred to as the "transferee") in circumstances to which paragraph (*f*) of the definition "disposition" in subsection (1) applies, without affecting the personal liabilities under this Act of the trustees of either trust or the application of subsection 104(5.8) and paragraph 122(2)(*f*), the transferee is deemed to be after the particular time the same trust as, and a continuation of, the transferor.

Trusts to ensure obligations fulfilled

(25.2) Where at any time property is transferred to a trust in circumstances to which paragraph (*j*) of the definition "disposition" in subsection (1) applies, the trust is, except for the purposes of subsection 104(1), deemed to deal with the property as agent for the transferor throughout the period that begins at the time of the transfer and ends at the time of the first change after that time in the beneficial ownership of the property.

Cost of trust interest

(25.3) If a trust (other than a personal trust or a prescribed trust) issues particular units of the trust to a taxpayer directly in satisfaction of a right to an amount payable from the trust in respect of the taxpayer's capital interest in the trust and subparagraph 53(2)(*h*)(i.1) applies in respect of the amount so payable, or would apply if that subparagraph were read without reference to clauses (A) and (B) of that subparagraph, the cost to the taxpayer of the particular units is deemed to be equal to the amount so payable.

(4) Subsection (1) applies after December 23, 1998.

(5) The definition "disposition" in subsection 248(1) of the Act, as enacted by subsection (2), applies to transactions and events that occur after December 23, 1998.

(6) The definitions "*alter ego* trust" and "joint spousal trust" in subsection 248(1) of the Act, as enacted by subsection (2), apply to trusts created after 1999.

(7) The definition "post-1971 spousal trust" in subsection 248(1) of the Act, as enacted by subsection (2), applies to trusts created after 1971.

(8) Subsections 248(25.1) and (25.2) of the Act, as enacted by subsection (3), apply to transfers that occur after December 23, 1998.

(9) Subsection 248(25.3) of the Act, as enacted by subsection (3), applies to the 1999 and subsequent taxation years.

29. (1) Section 250 of the Act is amended by adding the following after subsection (6):

Residence of *inter vivos* trusts

(6.1) For the purposes of provisions of this Act that apply to a trust for a taxation year only where the trust has been resident in Canada throughout the year, where a particular trust ceases at any time to exist and the particular trust was resident in Canada immediately before that time, the particular trust is deemed to be resident in Canada throughout the period that begins at that time and ends at the end of the year.

(2) Subsection (1) applies to the 1990 and subsequent taxation years.

30. (1) The Act is amended by adding the following after section 250:

Non-resident person's taxation year and income

250.1 For greater certainty, unless the context requires otherwise

(*a*) a taxation year of a non-resident person shall be determined, except as permitted by the Minister, in the same manner as the taxation year of a person resident in Canada; and

(*b*) a person who is non-resident at any time in a taxation year is a person for whom income for the year is determined in accordance with this Act.

(2) Subsection (1) applies after ANNOUNCEMENT DATE.

31. (1) Subsection 251(1) of the Act is amended by striking out the word "and" at the end of paragraph (*a*) and by replacing paragraph (*b*) with the following:

(*b*) a taxpayer and a personal trust are deemed not to deal with each other at arm's length if the taxpayer, or any person not dealing at arm's length with the taxpayer, would be beneficially interested in the trust if subsection 248(25) were read without reference to subclauses 248(25)(*b*)(iii)(A)(II) to (IV); and

(*c*) where paragraph (*b*) does not apply, it is a question of fact whether persons not related to each other are at a particular time dealing with each other at arm's length.

(2) Subsection (1) applies after December 23, 1998, except that paragraph 251(1)(*b*) of the Act, as enacted by subsection (1), shall, for the purpose of applying the definition "taxable Canadian property" in subsection 248(1) of the Act, not apply in respect of property acquired before December 24, 1998.

32. (1) The Act is amended by adding the following after section 253:

Investments in limited partnerships

253.1 For the purposes of subparagraph 108(2)(*b*)(ii), paragraphs 130.1(6)(*b*), 131(8)(*b*) and 132(6)(*b*), the definition "private holding corporation" in subsection 191(1) and regulations made for the

purposes of paragraphs 149(1)(*o*.3) and (*o*.4), a trust or corporation that holds an interest as a limited partner in a limited partnership is deemed

(*a*) to undertake an investing of its funds because of its acquisition and holding of the interest; and

(*b*) not to carry on any business or other activity of the partnership because of being a limited partner of that partnership.

(2) Subsection (1) applies after 1992.

Explanatory Notes

PREFACE

These explanatory notes describe, for discussion purposes, proposed amendments to the *Income Tax Act*. The proposed amendments are described, clause by clause, for the assistance of Members of Parliament, taxpayers and their professional advisors.

The Honourable Paul Martin
Minister of Finance

These explanatory notes are provided to assist in an understanding of proposed amendments to the *Income Tax Act*. These notes are intended for information purposes only and should not be construed as an official interpretation of the provisions they describe.

Clause 1

ITA
13(21)

"disposition of property"

Subsection 13(21) of the *Income Tax Act* defines the expression "disposition of property" for the purposes of the depreciation recapture rules in section 13.

The definition is repealed, strictly as a consequence of the introduction of the new definition "disposition" in subsection 248(1).

This amendment applies to transactions and events that occur after December 23, 1998.

Clause 2

ITA
40(2)(*g*)(iv)(A)

Paragraph 40(2)(*g*) of the Act denies the recognition of losses arising from certain dispositions, including dispositions by a taxpayer to a trust governed by a deferred profit sharing plan, employees profit sharing plan or registered retirement income fund, under which the taxpayer is a beneficiary.

Clause 40(2)(*g*)(iv)(A) is amended to replace a cross-reference to such trusts with a description of them. This amendment is strictly consequential on the replacement of the definition "disposition" in section 54 with a new definition of the same expression in subsection 248(1).

This amendment applies to the 1998 and subsequent taxation years.

Clause 3

ITA
43

Section 43 of the Act is a rule governing the disposition of a part of a property. For the purpose of computing a taxpayer's gain or loss from the disposition of a part of a property, a portion of the adjusted cost base (ACB) of the whole property must be allocated to the part on a reasonable basis.

Existing section 43 is renumbered as subsection 43(1) strictly as a consequence of the introduction of new subsection 43(2). This amendment applies to dispositions that occur after 1999.

New subsection 43(2) applies where part of a capital interest in a trust would, but for paragraph (*g*) or (*h*) of the definition "disposition" in subsection 248(1), be disposed of solely because of a satisfaction of a right to enforce a payment from the trust. No portion of the ACB of the taxpayer's capital interest is allocated to such a right. Accordingly, the ACB to the taxpayer of the remaining part of the taxpayer's capital interest in the trust is not reduced after the satisfaction of such a right. This amendment applies to satisfactions of rights that occur after 1999.

EXAMPLE

Joseph buys 1,000 units of XYZ Mutual Fund on December 23, 2000 for $10,000. XYZ has not made an election under subsection 132.11(1) to have a December 15 year end. XYZ makes $400 of its income for its 2000 taxation year payable to Joseph on December 31, 2000. However, without making any cash distribution of the income, XYZ issues 42 additional units on that date in satisfaction of the $400 of income payable. In November 2001, Joseph disposes of his 1,042 units for $10,700.

Results:

1. Under subsection 104(13), Joseph is required to include $400 in computing his income for the 2000 taxation year.

2. The right to enforce the payment of the distribution is treated as part of Joseph's capital interest in the trust under subsection 108(1). However, under paragraphs (g) and (h) of the definition "disposition" in subsection 248(1), there is no disposition of the capital interest on the satisfaction of the right.

3. Under subsection 43(2), the ACB allocated to the right to the income payable is nil. This ensures that the ACB of Joseph's 1,000 units will be $10,000 once the right to that income is satisfied, notwithstanding that Joseph acquired the units late in the 2000 taxation year.

4. The 42 additional units are acquired for $400. Consequently, the total ACB of the 1,042 units at the time of the disposition is $10,400. (Note: new subsection 248(25.3) ensures that there is an additional cost of $400 even if units are issued directly in satisfaction of the income payable.)

5. Consequently, the capital gain realized on the subsequent disposition of all of the units is $300.

The introduction of subsection 43(2) is part of a set of amendments designed to clarify the tax consequences of distributions from trusts to their beneficiaries after 1999. For the large part, the end results achieved under these rules are intended to accord with existing income tax practice. Other related amendments include the repeal of subsection 52(6), amendments to subsections 107(2) and (2.1), the amended definition of "capital interest" in subsection 108(1), paragraphs (*d*), (*g*) and (*h*) of the definition "disposition" in subsection 248(1) and new subsection 248(25.3). For further detail, see the commentary on those provisions.

Clause 4

ITA
49(5)(*b*)

Subsection 49(5) of the Act sets out rules dealing with extensions or renewals of an option.

Subsection 49(5) is amended to change a cross-reference in the subsection to the definition "disposition" in section 54 to a corresponding cross-reference to the new definition "disposition" in subsection 248(1).

This amendment applies to options granted after December 23, 1998.

Clause 5

ITA
52(1) and (1.1)

Subject to a number of exceptions, subsection 52(1) of the Act provides that, where an amount in respect of the value of a property has been included in computing a taxpayer's income, that amount is added in determining the cost to the taxpayer of the property for the purposes of determining capital gains and losses in respect of the property. Subsection 52(1.1) provides a similar rule in respect of taxable Canadian property of non-residents, except that it refers to a taxpayer's taxable income earned in Canada (as well as any amount subject to Part XIII withholding tax) instead of a taxpayer's income. Those subsections do not apply to rights to enforce payments from a trust that are described in subsection 52(6).

Subsection 52(1) is amended and subsection 52(1.1) is repealed so that subsection 52(1) applies to all taxpayers, whether resident in Canada or not. Amended subsection 52(1) generally applies where a taxpayer acquired property and an amount in respect of its value was included in computing the taxpayer's income for a taxation year throughout which the taxpayer was resident in Canada (or in computing a non-resident taxpayer's taxable income earned in Canada under section 115, taxable income under section 114 or an amount from which tax is withheld under Part XIII).

The exceptions in existing subsection 52(1) also generally apply for the purposes of amended subsection 52(1). However, the exception relating to rights to enforce payments from a trust is eliminated as a consequence of the repeal of subsection 52(6) described in the commentary below. Instead, amended subsection 52(1) excepts property that is a beneficiary's right to enforce payments by a trust or that is acquired in satisfaction of a beneficiary's "capital interest" in the trust (as defined in amended subsection 108(1)).

These amendments apply after 1999, except with respect to property that is acquired before 2000 and disposed of before March 2000.

ITA
52(6)

Subsection 52(6) of the Act provides that, where a right to enforce payment by a trust of an amount out of the trust's capital gains or income (determined without reference to the provisions of the Act) for the trust's taxation year is acquired by a trust beneficiary in the year, the beneficiary's cost of the right is the amount that became so payable. This ensures that there is generally no capital gain realized where a payment is made in satisfaction of such a right.

Subsection 52(6) is being repealed. Instead, rights to which subsection 52(6) apply are now generally treated as part of a taxpayer's "income interest" or "capital interest" in a trust (as those expressions are defined in subsection 108(1)). Where the right is part of a taxpayer's capital interest in a trust, the satisfaction of the right by way of a distribution by the trust will generally not constitute a disposition of that interest because of new paragraph (*g*) or (*h*) of the definition "disposition" in subsection 248(1). In addition, under existing paragraph 53(2)(*h*), a distribution in satisfaction of such a right generally will not result in a reduction of the adjusted cost base of that interest. In the event that such a right is capitalized by way of the issue of new trust units, new subsection 248(25.3) expressly provides for the cost of the new units.

The repeal of subsection 52(6) and the related amendments (described above) are designed to clarify the tax consequences of distributions from trusts to their beneficiaries after 1999. For the large part, the end results achieved under these rules are intended to accord with existing income tax practice.

The repeal of subsection 52(6) applies after 1999, except with respect to property that is acquired before 2000 and disposed of before March 2000.

Clause 6

ITA
53(2)(*h*)

Under paragraph 53(2)(*h*) of the Act, certain amounts are deducted in computing the adjusted cost base (ACB) to a beneficiary of the beneficiary's capital interest in a trust (other than an interest in a personal trust acquired for no consideration or an interest in a trust described in any of paragraphs (*a*) to (*d*) of the definition "trust" in subsection 108(1)). Trusts described in these paragraphs are generally those deemed to exist for income tax purposes and those that relate to employee compensation and retirement savings. Among the deducted amounts (as described in subparagraph 53(2)(*h*)(i.1)) are certain amounts payable to a trust beneficiary in respect of the beneficiary's capital interest in a trust, otherwise than as proceeds of disposition.

Paragraph 53(2)(*h*) is amended to ensure that it does not apply to interests in trusts described in paragraphs (*e*) and (*e*.1) of the definition "trust" in subsection 108(1). Trusts referred to in these two paragraphs are cemetery care trusts, trusts governed by eligible funeral arrangements and trusts each of the beneficiaries of which is an employee compensation trust, retirement savings trust or related segregated fund trust. This amendment corrects a legislative oversight.

Paragraph 53(2)(*h*) is also amended so that it does not apply to an interest in a personal trust that has never been acquired for consideration. New paragraph 108(6)(*c*) and new subsection 108(7) are relevant for the purpose of determining when an interest in a trust is considered to have been acquired for consideration.

These amendments apply to amounts that become payable after 1999.

ITA
53(2)(*i*) and (*j*)

Paragraphs 53(2)(*i*) and (*j*) of the Act set out certain reductions required to be made in determining the adjusted cost base (ACB) of a capital interest in a non-resident trust (including a unit of a non-resident unit trust) acquired by a purchaser. The ACB reduction in respect of a capital interest in a trust occurs, in general terms, where the purchaser acquired the interest from a non-resident person and assets of the trust consist primarily of any combination of taxable Canadian properties, Canadian resource properties, timber resource properties and income interests in trusts resident in Canada. The ACB reduction reduces the overall tax advantages associated with the

sale of such capital interests by reducing the ACB to the purchaser of the capital interest. The ACB reduction takes into account the deferral of the recognition of gains on such properties that used to result when a capital interest in a trust holding such properties (rather than the underlying properties) was sold by a non-resident person.

Paragraphs 53(2)(*i*) and (*j*) are amended so that such ACB reductions are no longer required in connection with purchases of a capital interest in a trust, where the interest is taxable Canadian property to the non-resident vendor. This amendment, which is relevant to purchases after April 26, 1995, is consequential to the extension of taxable Canadian property (under former subsection 115(1) and the new definition "taxable Canadian property" in subsection 248(1)) to include capital interests in a non-resident trust in cases where the trust's assets consist primarily of taxable Canadian properties and other properties described above.

ITA
53(4)

Subsection 53(4) of the Act provides rules that affect the computation of the adjusted cost base (ACB) to a taxpayer of any "specified property". As defined in section 54, "specified property" is capital property that is a share, a capital interest in a trust, a partnership interest or an option to acquire any such property. The rules in subsection 53(4) apply where the proceeds of disposition of a specified property are determined under any one of a number of provisions in the Act set out in the subsection. Where this is the case and the ACB of the specified property was reduced under paragraph 53(2)(*g*.1) as a consequence of a forgiveness of debt, the ACB continues to be reduced under that paragraph as a consequence of the operation of subsection 53(4). The only significance of this reduction is with respect to the potential future application of section 80.03 which, in certain cases, recaptures reductions previously made under paragraph 53(2)(*g*.1) in computing the ACB of specified property on a future disposition of such property.

Subsection 53(4) is amended to add a reference in the subsection to paragraph 107.4(3)(*a*). Subsection 107.4(3) provides for a rollover on certain transfers of property that do not involve any change in the beneficial ownership of the property. As a result, the ACB of a property transferred to a trust that was subject to a reduction because of the forgiveness of debt rules continues to be reduced on the same basis if the property is transferred in circumstances where proceeds of disposition are determined under paragraph 107.4(3)(*a*).

This amendment applies to the 1998 and subsequent taxation years.

Clause 7

ITA
54
"disposition"

The expression "disposition" is defined, for the purposes of the capital gains rules, in section 54 of the Act.

The definition is repealed strictly as a consequence of the introduction of the new definition "disposition" in subsection 248(1).

The repeal of this definition applies to transactions and events that occur after December 23, 1998.

Clauses 8 and 9

ITA
59(5) and 66.4(5)
"disposition"

Subsections 59(5) and 66.4(5) of the Act define the expressions "disposition" and "proceeds of disposition" for the purposes of sections 59 and 66.4. These expressions are defined in the same way as they are defined in section 54.

Subsections 59(5) and 66.4(5) are amended to eliminate the references to the expression "disposition", as this expression is now defined in subsection 248(1).

These amendments apply to transactions and events that occur after December 23, 1998.

Clause 10

ITA
69(1)(*b*) and (*c*)

Subsection 69(1) of the Act provides rules that deal with gifts and non-arm's length dispositions of property, except where such transactions are covered by other express provisions in the Act (e.g., section 85, subsections 107(2) and (2.1) and new subsection 107.4(3)). Under paragraph 69(1)(*b*), a taxpayer is deemed to receive proceeds of disposition equal to the fair market value of the property disposed of where the taxpayer disposed of the

property by way of gift or to a non-arm's length person for proceeds less than the fair market value of the property. Under paragraph 69(1)(*c*), a taxpayer who has acquired property by way of gift, bequest or inheritance is deemed by paragraph 69(1)(*c*) to have acquired the property at its fair market value.

Paragraph 69(1)(*b*) is amended to ensure that, subject to subsection 107.4(3), it applies to a disposition to a trust of a property where no change in the beneficial ownership of the property is involved.

Paragraph 69(1)(*c*) is amended so that a taxpayer, where subsection 69(1) applies, is also considered to acquire property at its fair market value where the acquisition is because of a disposition that does not result in any change in the beneficial ownership of the property.

For a description of circumstances where a transfer without any change in beneficial ownership is not a "disposition", reference should be made to the commentary on the new definition "disposition" in subsection 248(1).

These amendments apply after December 23, 1998.

Clause 11

ITA
70(5.3)

Subsection 70(5) of the Act provides for the deemed disposition of a taxpayer's capital property on the taxpayer's death for proceeds equal to the property's fair market value immediately before the death. In the event that the property includes shares and there was a life insurance policy under which the taxpayer's life was insured, the fair market value of the shares is determined under subsection 70(5.3) as if the value of the policy were the policy's cash surrender value immediately before the taxpayer's death. The purpose of subsection 70(5.3) is to ensure that life insurance proceeds payable as a consequence of death are not reflected in share value and therefore do not give rise to a capital gain on death.

Existing subsection 104(4) provides, in certain cases specified, for a deemed disposition of capital property (which includes shares) on the death of a taxpayer for proceeds equal to the property's fair market value. Existing section 128.1 also provides, in certain cases, that property (including shares) is deemed to be disposed of by an

individual for its fair market value in the event that the individual becomes or ceases to be resident in Canada.

Subsection 70(5.3) is amended so that it also applies for the purposes of subsection 104(4) and section 128.1. As a consequence, where property is deemed by subsection 104(4) to have been disposed of by a trust as a consequence of the death of an individual and there is a life insurance policy under which the individual's life is insured, the fair market value of the property is determined for the purposes of subsection 104(4) as if the value of the policy were the policy's cash surrender value immediately before the death. Similarly, where property is deemed by section 128.1 to have been disposed of by an individual as a consequence of the individual becoming or ceasing to be resident in Canada and there is a life insurance policy under which the individual's life is insured, the fair market value of the property is determined for the purposes of section 128.1 as if the value of the policy were the policy's cash surrender value immediately before the individual became or ceased to be resident in Canada.

Subsection 70(5.3) is also amended so that it applies in determining the fair market value of any property (e.g., an interest in a trust or a partnership), not just shares.

Subsection 70(5.3) is further amended to remove references to former subsections 70(9.4) and (9.5), given that these subsections have been repealed.

These amendments apply to dispositions that occur after October 1, 1996.

ITA
70(9.1) and (9.3)

Subsections 70(9.1) and (9.3) of the Act permit farm property (including shares of, or interests in, family farm corporations and family farm partnerships) to be disposed of on a rollover basis from a spousal trust to the children of the settlor of the spousal trust.

Subsections 70(9.1) and (9.3) are amended to preserve the existing rollover. These amendments are strictly consequential to changes to the rules in subsection 73(1) that govern rollovers to spousal trusts.

These amendments apply to dispositions after 1999.

Clause 12

ITA
73(1) to (1.02)

Subsection 73(1) of the Act generally provides for a tax-free disposition of capital property where it is transferred by an individual to the individual's spouse or to a spousal trust (i.e., essentially a trust for the exclusive benefit of the spouse during the spouse's lifetime). For subsection 73(1) to apply, the transferor and transferee must both be resident in Canada at the time of the transfer. Provision is made to elect out of the rollover rule, in which case the proceeds of disposition for the transferor would be deemed by subsection 69(1) to be not less than the fair market value of the property transferred. Where there has been a transfer to a spousal trust, subsections 104(4) and 107(4) ensure that capital gains are appropriately recognized by a deemed disposition of trust property at the time of the beneficiary spouse's death (or, where applicable, at the time of any earlier distribution to another beneficiary).

Subsection 73(1) is amended, in conjunction with the introduction of subsection 73(1.01), so that the current rules in subsection 73(1) for transfers by an individual to a trust are extended to similarly allow for a tax-free disposition:

- where the individual transfers property to a trust for the exclusive benefit of the individual during the individual's own lifetime (such a trust will generally be an "*alter ego* trust", as defined in subsection 248(1), in the event that the individual is at least 65 years of age), and

- where the individual transfers the property for the joint benefit of the individual and the individual's spouse during their lifetimes (such a trust will generally be a "joint spousal trust", as defined in subsection 248(1), in the event that the individual is at least 65 years of age).

However, new subsection 73(1.02) limits the application of subsection 73(1.01). It provides that, in order for subparagraphs 73(1.01)(*c*)(ii) and (iii) to apply to a transfer of property by an individual to a trust, the following conditions must be met:

- the trust was created after 1999,

- the individual has attained 65 years of age at the time of the creation of the trust, except where no person (other than the individual) or partnership has any absolute or contingent right as a

beneficiary under the trust (determined with reference to subsection 104(1.1)), and

- subject to the same exception, the transfer was not part of a series of transactions or events that includes a transfer of property to the transferor (or the spouse or former spouse of the transferor) from a trust (other than a testamentary trust) in circumstances to which subsection 107(2) applied, where one of the main purposes of that series can reasonably be considered to avoid the deemed disposition of trust property under subsection 104(4) or (5) on a day determined under paragraph 104(4)(*b*) or (*c*).

The purpose of the "age 65" restriction (above and in amended subsection 104(4)) is to limit the opportunity to engage in tax planning involving trusts and the maximization of the deferral of the recognition of capital gains. For example, a 66 year old parent might arrange for common shares of a private corporation to be issued to his or her 27 year old child with the understanding that those common shares be transferred by the child into a trust effectively controlled by the parent which provides for beneficiaries after the child's death. The purpose of this arrangement may, in part, be to minimize capital gains otherwise recognized on the death of the parent. In these circumstances, the transfer by the child to the trust cannot be made on a rollover basis and subsection 104(4) generally provides for a deemed disposition on the 21st anniversary of the trust (rather than on the child's death).

The purpose of the last restriction is consistent with the purpose of the "age 65" restriction. Assume there is an upcoming 21-year anniversary for a trust the beneficiaries of which are a 66 year old parent and the adult children of the parent. Property is transferred to the parent alone (rather than to both the parent and the beneficiaries) on the understanding that the parent will transfer the property back to a trust with the same beneficiaries. In the absence of the last restriction, the transactions described would result in an inappropriate extension of the 21-year rule for deemed dispositions of trust property.

Changes to subsections 104(4) and (6) and 107(4), as described in the commentary below, have been made so that the income tax regime for trusts to which transfers have been made under amended section 73 parallel the existing rules for spousal trusts.

Under amended subsection 73(1), an election is still available in the event that a transferor does not wish to have property transferred on a rollover basis. However, the use of this election is not relevant for the purposes of amended subsections 104(4) and 107(4) and new subsection 107.4(1).

These amendments apply to transfers that occur after 1999.

ITA
73(1.1)

Subsection 73(1.1) of the Act generally provides that one spouse is considered to have transferred property to another spouse where the other spouse obtains the property under provincial law because of a decree, order or judgment of a competent tribunal. The rule applies for the purpose of the rollover rule in subsection 73(1).

Subsection 73(1.1) is amended to change a number of cross-references, to reflect amended subsection 73(1) and new subsection 73(1.01) (described in the commentary above).

This amendment applies to transfers that occur after 1999.

Clause 13

ITA
75(3)(*a*)

Subsection 75(3) of the Act exempts certain trusts from the application of subsection 75(2), which generally provides for the attribution of income from a trust property to a person resident in Canada where that property was received by the trust from the person and can revert to the person (or pass to other persons determined by that person).

Paragraph 75(3)(*a*) is amended to extend the exemption to trusts governed by retirement compensation arrangements (as defined in subsection 248(1)). These trusts are subject to tax in the hands of the trustee under Part XI.3. This amendment ensures that these trusts will not also be subject to tax under Part I in the hands of a person (typically an employer) who made contributions to the trust.

This amendment applies to taxation years ending after October 8, 1986, the date on which the retirement compensation arrangement rules were originally announced.

Clause 14

ITA
94(1)(*c*)(i)(B) and (D)

Where certain conditions are met, a non-resident discretionary trust to which existing section 94 of the Act applies is generally treated as a trust resident in Canada the taxable income of which is the total of its taxable income earned in Canada (computed on the assumption that the trust was non-resident) and two other amounts. One of these other amounts for a taxation year is described in clause 94(1)(*c*)(i)(B) as the amount that would be the trust's foreign accrual property income for the year if paragraph 94(1)(*d*) applied. Under paragraph 94(1)(*d*), a trust is treated as a corporation for the purpose of computing foreign accrual property income.

Clause 94(1)(*c*)(i)(B) is amended so that the amount determined under that clause in respect of a trust for a taxation year is generally the trust's foreign accrual property income for the year, determined on the assumptions that the trust is a non-resident corporation and that all of the shares of the capital stock of that corporation are owned by a person resident in Canada. Exceptions to this general rule are described below.

Clause 94(1)(*c*)(i)(B) is also amended to clarify that the 21-year deemed disposition rule for trusts applies for the purpose of computing the amount determined under clause 94(1)(*c*)(i)(B), despite the fact that the rule applies to trusts and not to corporations. This clarification applies to disposition dates determined after 1998.

Subclause 94(1)(*c*)(i)(B)(II) is introduced so the exclusion in the definition "foreign accrual property income" for dividends from other foreign affiliates does not apply for the purpose of computing the amount determined under clause 94(1)(*c*)(i)(B). This reflects the fact that a trust that receives such dividends would be expected to ultimately distribute such dividends as trust capital. This measure applies to dividends received after 1998.

Under the definition "foreign accrual property income", taxable capital gains and allowable capital losses that have accrued after the 1975 taxation year and relate to "excluded property" are generally disregarded. Subclause 94(1)(*c*)(i)(B)(III) is introduced so that the disregarding of "excluded property" does not apply for the purpose of determining the amount determined under clause 94(1)(*c*)(i)(B). This reflects the fact that a distribution of gains of this nature would also be expected to be distributed as trust capital. This measure applies to dispositions that occur after 1998.

Subclause 94(1)(*c*)(i)(B)(IV) is introduced so that section 94.1 is no longer relevant for the purposes of determining the amount under clause 94(1)(*c*)(i)(B). Instead, new clause 94(1)(*c*)(i)(D) adds the amount determined under that section in respect of a trust in computing the trust's taxable income under subparagraph 94(1)(*c*)(i).

These amendments come into effect in the manner indicated in the commentary above and apply to the 1999 and subsequent taxation years. However, as announced in the 1999 budget, further amendments to this section are contemplated.

Clause 15

ITA
104(1) and (1.1)

Subsection 104(1) of the Act provides that a reference to a trust or estate is read in the Act as a reference to the trustee or the executor, administrator, heir or other legal representative having ownership or control over trust property.

Subsection 104(1) is amended so that this rule does not apply where the context otherwise requires and to clarify that this rule is merely meant to be a convenient way of linking the trustees and others described in the subsection with a trust for the purposes of the Act. This amendment recognizes that there are references to "trust" in the Act that are meant to indicate a trust arrangement, rather than the persons who are responsible for the operation of the arrangement. The latter references include those found in subsections 74.4(4), 104(5.3) and (5.5), 108(6) and 127(7).

Subsection 104(1) is amended, in conjunction with 104(1.1), so that references in the Act to trusts are generally not considered to include an arrangement where a trust can reasonably be considered to act as agent for its beneficiaries with respect to all dealings in all of the trust's property. These arrangements are generally known as "bare trusts". Trusts described in paragraphs (*a*) to (*e*.1) of the definition "trust" in subsection 108(1) are expressly not affected by this amendment.

New subsection 104(1.1) applies for the purpose of identifying beneficiaries under a trust for the purpose of subsection 104(1), as well as for the purposes of subparagraph 73(1.02)(*b*)(ii) and paragraph 107.4(1)(*e*). A person or partnership is deemed not to be a beneficiary under a trust at a particular time for these purposes where the person or partnership is beneficially interested in the trust at the

particular time solely because of any one, or a combination of, the following:

- a right that may arise as a consequence of the terms of the will or other testamentary instrument of an individual who, at the particular time, is a beneficiary under the trust,
- a right that may arise as a consequence of the law governing the intestacy of an individual,
- a right as a shareholder under the terms of the shares of the capital stock of a corporation that, at the particular time, is a beneficiary under the trust, or
- a right as a member of a partnership under the terms of the partnership agreement, where, at the particular time, the partnership is a beneficiary under the trust.

These amendments generally apply to the 1998 and subsequent taxation years. However, in order to co-ordinate this amendment with changes to the replacement of the definition "disposition" in section 54 with the new definition of the same expression in subsection 248(1), it does not apply in connection with transfers of property that occurred before December 24, 1998.

ITA
104(4) to (5.2)

Subsections 104(4) to (5.2) of the Act set out what is generally referred to as the "21-year deemed realization rule" for trusts. The purpose of the rule is to prevent the use of trusts to defer indefinitely the recognition for tax purposes of gains accruing on capital properties, resource properties and land inventories. These subsections generally treat such properties as having been disposed of and reacquired by trusts (other than spousal trusts) every 21 years at the properties' fair market value. The first deemed disposition day for post-1971 spousal trusts, as provided under paragraph 104(4)(*a*), is the day on which the spouse beneficiary dies. The fair market value of property that is deemed to be disposed of on a day determined under paragraph 104(4)(*a*) or (*a*.1), is determined with reference to the valuation rule for insurance policies in amended subsection 70(5.3) (see the commentary above on that provision).

Subsections 104(4) to (5.2) are amended so that the deemed realization rules do not apply to "exempt property" of a non-resident trust, as the expression is now defined in subsection 108(1). "Exempt property" is defined as property the income or gain from the disposition of which by a taxpayer is exempt

from Canadian taxation for the taxpayer either because the taxpayer is not resident in Canada or because of a tax treaty. The purpose of this amendment is to prevent the deemed realization rules from being used to increase the cost of such property. The increased cost might be relevant in the event that a non-resident trust distributes such property to Canadian beneficiaries. These amendments apply to deemed disposition days that are after December 23, 1998. In the case of capital property (other than depreciable property), the amendments also apply to deemed disposition days that are after 1992, but only for the purpose of determining after December 23, 1998 the cost amount to a trust of property.

Paragraph 104(4)(*a*) is amended to provide the first deemed disposition day in respect of an *inter vivos* trust created after 1999 that at any time after 1999 was a trust for the exclusive benefit of the settlor during the settlor's lifetime (i.e. an "*alter ego* trust", as newly defined in subsection 248(1)) or a trust for the joint benefit of the settlor and the settlor's spouse during their lifetimes (i.e. a "joint spousal trust", as newly defined in subsection 248(1)). The first deemed disposition date in these circumstances, in the event that the settlor was at least 65 years of age at the time of the settlement, is the day on which the settlor dies (or, in the case of a trust for the joint benefit of the settlor and spouse, the day on which the survivor dies). This amendment applies to the 2000 and subsequent taxation years. For an explanation of the age 65 restriction, see the commentary on new subsection 73(1.02).

Paragraph 104(4)(*a*.2) is introduced to provide for a deemed disposition day for a trust that distributes property financed by a liability of the trust. This measure only applies, however, if one of the purposes of the transaction was to avoid taxes otherwise payable as a consequence of the death of an individual. The deemed disposition under this paragraph occurs immediately after the distribution of the property (as the determination is made as if a day had ended immediately after each distribution). This amendment applies to deemed disposition days determined after Announcement Date.

Paragraph 104(4)(*a*.3) is introduced to provide for a deemed disposition day for a trust in the event that an individual, after Announcement Date, has transferred property to the trust in circumstances to which subsection 73(1) applies, it is reasonable to conclude that the property was so transferred in anticipation that the taxpayer would subsequently cease to reside in Canada and the individual subsequently ceases to reside in Canada. This measure does not apply, however, to property transferred that is exempt under amended subparagraphs 128.1(4)(*b*)(i) to (iii) from a deemed disposition on the transferor's emigration. The deemed disposition

under paragraph 104(4)(*a*.3) occurs immediately after the individual ceases to be resident in Canada.

Paragraph 104(4)(*c*) is amended so that there is not a deemed disposition day for a trust 21 years after any day determined under new paragraph 104(4)(*a*.2) or (*a*.3). This amendment applies to the 2000 and subsequent taxation years.

ITA
104(5.3)(*c*) and (*d*)

Subsection 104(5.3) of the Act allowed the deferral of the 21-year deemed disposition date (determined under paragraph 104(4)(*a*.1) or (*b*)) for certain family trusts. The measure has already been terminated under the existing rules, so that the deferred disposition date was no later than January 1, 1999.

Subject to paragraph 104(5.3)(*d*), paragraph 104(5.3)(*c*) ensures that the deemed disposition date cannot be deferred beyond January 1, 1999 (or an earlier date, where applicable) through a transfer of property from one trust to another that does not constitute a "disposition" because of existing paragraph (*e*) of the definition "disposition" in section 54.

Any trust-to-trust transfer in the period (referred to below as the "relevant period") that is after the original date of the deemed disposition and before the date of the deferred deemed disposition is considered to be a "disposition" (i.e., a taxable event) for a trust that has made an election under subsection 104(5.3). Paragraph 104(5.3)(*d*) provides for relief from paragraph 104(5.3)(*c*) where, essentially, one trust is replaced by another trust with the same terms and beneficiaries. In this case, the new trust is deemed to be the same trust as, and a continuation of, the original trust.

Paragraph 104(5.3)(*c*) is amended to eliminate the reference to the existing definition of "disposition" in section 54, as a consequence of the repeal of that definition and its replacement by a new definition of "disposition" in subsection 248(1).

Paragraph 104(5.3)(*c*) is also amended so that it only applies where there is a "disposition" of property (as now defined in subsection 248(1)). The only relevant "trust-to-trust" transfer where there is no "disposition" is one to which paragraph (*f*) of the new definition "disposition" applies. Where paragraph (*f*) of that definition applies, the transferee trust is considered under subsection 248(25.1) to be the same as and a continuation of the transferor trust.

Paragraph 104(5.3)(*d*) is repealed, consequential on the introduction of paragraph (*f*) of the new definition "disposition" and new subsection 248(25.1).

These amendments apply to transfers made after December 23, 1998.

ITA
104(5.8)

Subsection 104(5.8) of the Act is a special rule designed to prevent the avoidance of the 21-year rule through the use of trust-to-trust transfers that do not involve dispositions of property at fair market value. Subsection 104(5.8) generally provides for a transferee trust to assume the next deemed disposition day of the transferor, if that day is earlier than the transferee's next deemed disposition day. In the case of spousal trusts under which the beneficiary spouse is still alive, subsection 104(5.8) provides a deemed disposition as soon as the transfer is completed unless relief is provided under paragraph 104(5.8)(*b*). Paragraph 104(5.8)(*b*) provides relief where both the transferor and transferee trusts are spousal trusts to which paragraph 104(4)(*a*) or (*a*.1) applies and under which the spouse beneficiary is alive.

Subsection 104(5.8) is amended to eliminate a reference to trust transfers under paragraph (*e*) of the definition "disposition" in section 54, as a consequence of the repeal of that definition. Subsection 104(5.8) is also amended so that it now covers transfers under new paragraph (*f*) of the definition "disposition" in subsection 248(1) and under new subsection 107.4(3). These amendments apply to any transfers that were made after December 23, 1998.

Subsection 104(5.8) is amended so that it does not apply to transfers between trusts, if the transferee trust was, at the time of the transfer, described in paragraph (*g*) of the definition "trust" in subsection 108(1). This amendment, which is made as a consequence of the introduction of subparagraph (*g*)(iv) of that definition, applies only to transfers made after February 11, 1991 and before December 24, 1998. Subparagraph (*g*)(iv) of that definition has the effect of limiting an exemption from the 21-year deemed disposition rule for a trust in which interests are vested indefeasibly, in the event that non-resident beneficiaries own more than 20% of the interests in the trust.

Subparagraph 104(5.8)(*a*)(i) is amended to ensure that the determination of a deemed disposition day for a transferee trust will not preclude any earlier deemed disposition day under new paragraph 104(4)(*a*.2) or (*a*.3). This amendment applies to transfers made after Announcement Date.

Subsection 104(5.8) is further amended to extend its existing rules for transfers from spousal trusts to transfers from other specified trusts. The additional trusts so specified are those created after 1999 by a settlor (aged 65 years or more) for the exclusive benefit of the settlor during the settlor's lifetime (i.e. an "*alter ego* trust", as newly defined in subsection 248(1)) or for the joint benefit of the settlor and the settlor's spouse during their joint lifetimes (i.e. a "joint spousal trust", as newly defined in subsection 248(1)) . Where the settlor of an *alter ego* trust is still alive (or, in the case of a joint spousal trust, where the settlor or the spouse is still alive), a deemed disposition day for the trust may occur once a transfer from the trust is completed. However, amended paragraph 104(5.8)(*b*) and new paragraphs 104(5.8)(*b*.1) and (*b*.2) provide for no deemed disposition day in the case of a transfer from one of the additional specified trusts where the transferee trust is also a specified trust to which paragraph 104(4)(*a*) applies and the settlor (or, in the case of a joint spousal trust, either the settlor or that spouse) is alive. These amendments apply to transfers after 1999. For further detail on new rules for *alter ego* trusts and joint spousal trusts, see the commentary on amended subsection 73(1) and paragraph 104(4)(*a*).

ITA
104(6)

Subsection 104(6) of the Act generally allows a trust to deduct an amount for a taxation year not exceeding its income for the year that became payable to its beneficiaries. However, in the case of spousal trusts there are restrictions designed to ensure that spousal trusts cannot claim a deduction under subsection 104(6) in respect of income allocated to non-spouse beneficiaries to the extent the income accrues during the lifetime of the spouse beneficiaries. (With regard to income for the year in which a spouse beneficiary dies, this restriction only applies in connection with income from dispositions of capital property, land inventory and Canadian and foreign resource property that occur before end of the deemed disposition day caused by the spouse's death.) There is also a restriction in subsection 104(6) designed to limit the extent to which a trust can claim a deduction in respect of distributions by the trust of amounts paid to the trust from the trust's NISA Fund No. 2 (as defined in subsection 248(1)).

Paragraph 104(6)(*a*.3) is introduced so that the restrictions with regard to a trust's NISA Fund No. 2 do not apply to any trust deemed to exist because of the special rules for communal organizations in section 143. This amendment applies to the 1998 and subsequent taxation years.

Paragraph 104(6)(*b*) is amended to extend the restrictions for spousal trusts to other specified trusts created after 1999. The trusts so specified are those created after 1999 by a settlor (aged 65 years or more) for the exclusive benefit of the settlor during the settlor's lifetime (i.e. an "*alter ego* trust", as newly defined in subsection 248(1)) or for the joint benefit of the settlor and the settlor's spouse during their joint lifetimes (i.e. a "joint spousal trust", as newly defined in subsection 248(1)). The restrictions for *alter ego* trusts apply until the death of the settlor. The restrictions for joint spousal trusts apply until the later of the death of the settlor and the spouse. For further detail on new rules for these specified trusts, see the commentary on amended subsection 73(1) and paragraph 104(4)(*a*). This amendment applies to the 2000 and subsequent taxation years.

Clauses 104(6)(*b*)(ii)(A) and (B) are amended to refer to a post-1971 spousal trust strictly as a consequence of the new definition of this term contained in subsection 248(1). For further detail, see the commentary on amended subsection 248(1). This amendment applies to the 2000 and subsequent taxation years.

Subparagraph 104(6)(*b*)(iii) is amended to extend the restrictions for deductions under subsection 104(6) in the taxation year in which the relevant beneficiary dies. The intended effect of the new restrictions is that post-1971 spousal trusts, *alter ego* trusts and joint spousal trusts cannot deduct an amount under subsection 104(6) in respect of income accrued up to the end of the deemed disposition day caused by the death of the spouse or other relevant beneficiary. This amendment applies to the 2000 and subsequent taxation years.

EXAMPLE

The spouse beneficiary of a post-1971 spousal trust dies in the 2001 taxation year of the trust. Before distribution to beneficiaries, the trust's total income for the year (determined without reference to any deemed disposition under subsection 104(4) and any deduction under subsection 104(6)) is $100, of which $20 is payable to the spouse prior to the spouse's death and of which the remaining $80 is payable to the surviving beneficiaries. $40 of the $100 income accrued before the spouse's death.

Results:

1. Under subparagraph 104(6)(b)(i) the trust's income for the year that became payable in the year to beneficiaries is $100.

2. The amount determined under subparagraph 104(6)(b)(iii) is $20 (i.e. [$100 - ($20 + $60)]).

3. The total amount deductible by the trust cannot exceed the amount by which the amount determined under subparagraph 104(6)(b)(i) exceeds the amount determined under subparagraph 104(6)(b)(iii).

4. Consequently, the trust's maximum deduction for the year is $80 (i.e. $100 - $20): the trust is not allowed a deduction in respect of the $20 portion of trust income accrued up to the end of the deemed disposition day caused by the spouse's death but payable only after the death.

ITA
104(13)

Subsection 104(13) of the Act sets out amounts included in computing the income of a beneficiary under a trust. Where a trust is not resident in Canada, paragraph 104(13)(*c*) provides that the beneficiary must include in computing income all amounts payable in respect of the beneficiary's interest in the trust, otherwise than as proceeds of disposition or amounts paid in satisfaction of the distribution of capital by a personal trust. There is uncertainty in this regard under the existing law, given that different types of distributions from a trust to a beneficiary might arguably be viewed as resulting in proceeds of disposition with respect to all or part of a beneficiary's interest in the trust.

Subsection 104(13) is amended so that it requires a beneficiary to include in income under that subsection only current income payable from a non-resident trust. For this purpose, a non-resident trust's income is intended to be determined in accordance with Canadian income tax rules. See also, in this regard, the commentary on new section 250.1.

This amendment applies to the 2000 and subsequent taxation years.

ITA
104(15)

Subsection 104(14) of the Act provides a mechanism under which a preferred beneficiary of a trust and the trust can elect to have a designated amount taxed in the hands of the beneficiary rather than at the trust level. Under the definition "preferred beneficiary" in subsection 108(1), a preferred beneficiary of a trust is generally a disabled person resident in Canada who is, or is closely related to, the

settlor of the trust. Under paragraph 104(15)(*a*), if the preferred beneficiary is the living spouse beneficiary under a spousal trust, an "allocable amount" in respect of the beneficiary for a taxation year is the trust's "accumulating income" for the year (which, in general terms, is defined in subsection 108(1) as undistributed trust income).

Subsection 104(15) is amended so that the preferred beneficiary election in connection with allocations of income from an *alter ego* trust, a joint spousal trust, a post-1971 spousal trust or a trust described in the definition "pre-1972 spousal trust" in subsection 108(1) is available to the spouse or other beneficiary (i.e., the settlor) identified in paragraph 104(4)(*a*), only while the spouse or the other beneficiary is alive.

This amendment applies to the 2000 and subsequent taxation years.

ITA
104(19)

Subsection 104(19) of the Act permits a trust to designate dividends received by it in a taxation year on shares of a taxable Canadian corporation to be taxable dividends received by a beneficiary of the trust, rather than by the trust itself, in the year from the corporation.

Subsection 104(19) of the Act is amended so that a trust will, except for the purposes of the dividend gross-up in paragraph 82(1)(*b*) and stop-loss rules in paragraphs 107(1)(*c*) and (*d*) and section 112, still be treated as having received the dividend even if it is designated in favour of a beneficiary. In most cases, the trust will be allowed a corresponding deduction under subsection 104(6) to offset the resulting income inclusion. However, as described in the commentary on amendments to subsection 104(6), there are certain restrictions under amended subsection 104(6) on the deduction of amounts made payable from *alter ego* trusts, joint spousal trusts and post-1971 spousal trusts.

This amendment applies to taxation years that end after 2000.

Clause 16

ITA
106(1.1)

Subsection 106(1.1) of the Act provides that, for the purposes of determining the deduction available under subsection 106(1) in respect of a beneficiary's income interest in a trust, the cost to

the beneficiary of the interest is nil except where the interest was acquired from a beneficiary under the trust.

Subsection 106(1.1) is amended so that the deemed nil cost also does not apply to a beneficiary's income interest in a trust where:

- any part of the interest was acquired from a person who was the beneficiary in respect of the interest immediately before that acquisition, or
- the cost of any part of the interest was ever determined not to be nil under the taxpayer migration rules in section 128.1.

Subsection 106(1.1) is also amended to ensure that it applies for the purposes of the Act, and not simply subsection 106(1).

These amendments apply to the 2000 and subsequent taxation years.

Clause 17

ITA
107(1)(*a*) and (*b*)

Subsection 107(1) of the Act contains special rules that apply to the disposition of a capital interest in a trust.

Paragraph 107(1)(*a*) applies for the purpose of computing a taxpayer's taxable capital gain from the disposition of a capital interest in a personal trust (or a prescribed trust described in section 4800.1 of the Regulations), except where the interest was an interest in a non-resident *inter vivos* trust purchased by the taxpayer and the disposition was not by way of a distribution to which subsection 107(2) applies.

Where paragraph 107(1)(*a*) applies, the adjusted cost base (ACB) to the taxpayer of a trust capital interest for capital gains purposes is generally equal to the greater of the ACB otherwise determined and the "cost amount" of the interest. Subsection 108(1) provides that, for this purpose, the "cost amount" of a capital interest at any time is based on the amount of the trust's money and the cost amount of the trust's other property. The "cost amount" mechanism in paragraph 107(1)(*a*) generally allows the flow-out from a personal or prescribed trust to a beneficiary of trust capital without adverse tax consequences. However, the concluding words in subsection 107(1) provide that paragraph 107(1)(*a*) generally does not apply with regard to certain purchased interests in non-resident trusts.

Paragraph 107(1)(*a*) is amended, in conjunction with the repeal of the concluding wording in subsection 107(1), to ensure that paragraph 107(1)(*a*) never applies to dispositions of any capital interests in non-resident trusts acquired for consideration. New paragraph 108(6)(*c*) and new subsection 108(7) are relevant in determining where an interest in a trust has been acquired for consideration. Amended paragraph 107(1)(*a*) also ensures that, for this purpose, a non-resident trust includes a trust deemed by subparagraph 94(1)(*c*)(i) to be resident in Canada.

Paragraph 107(1)(*b*) is repealed because it is unnecessary. Since paragraph 107(1)(*a*) applies only for the purposes of computing a taxpayer's capital gain, it is clear without paragraph 107(1)(*b*) that the ACB calculation in paragraph 107(1)(*a*) is not relevant for the purposes of computing a taxpayer's allowable capital loss.

These amendments apply to the 2000 and subsequent taxation years.

ITA
107(1.1)

Subsection 107(1.1) of the Act provides, for the purposes of subsection 107(1), that the cost of a capital interest in a trust is nil except where the interest is acquired from a previous capital beneficiary in the trust or where the interest is issued to the beneficiary for consideration equal to the fair market value of the interest at the time of issuance.

Subsection 107(1.1) is amended so that it applies only to trusts that are personal trusts or prescribed trusts. It is intended that trusts described in section 4800.1 of the Regulations be prescribed for this purpose.

Paragraph 107(1.1)(*b*) is amended to provide that the cost of the interest will not be deemed nil where:

- the cost of any part of the interest would otherwise be determined not to be nil under the taxpayer migration rules in section 128.1 or former section 48 or under paragraph 111(4)(*e*) (acquisition of control), or

- any part of the interest was acquired from a person who was the beneficiary in respect of the interest immediately before that acquisition.

Subsection 107(1.1) is also amended to ensure that it applies for the purposes of the Act, and not simply subsection 107(1).

These amendments apply to the 2000 and subsequent taxation years.

ITA
107(2), (2.001), (2.002) and (3)

Subsection 107(2) of the Act applies where a personal trust or a trust described in section 4800.1 of the Regulations distributes property to a beneficiary in satisfaction of all or part of the beneficiary's capital interest in the trust. Under paragraphs 107(2)(*a*) and (*b*), the trust is deemed to have disposed of the property for proceeds of disposition equal to the property's cost amount and the property is deemed to have been acquired by the beneficiary for the same amount plus a "bump" equal to the specified percentage of any excess of the adjusted cost base to the beneficiary of the capital interest over its "cost amount" (as defined by subsection 108(1)) to the beneficiary of the interest. Under paragraph 107(2)(*c*), the beneficiary is deemed to have disposed of the capital interest for proceeds equal to the deemed acquisition cost (determined as if the specified percentage referred to above were 100 per cent) less a reduction equal to the amount of debt assumed by the beneficiary that is conditional upon the distribution of the property. Under subsection 107(3), the specified percentage is 100 per cent in the case of non-depreciable capital property (e.g., land and shares) and 50 per cent in any other case.

Subsection 107(2) is amended to clarify that it applies in connection with distributions in respect of a capital interest in a personal or prescribed trust only if the distribution results in a "disposition" of all or part of the capital interest. Where the distribution does not constitute a "disposition" of a capital interest in a trust because of new paragraph (*h*) of the definition "disposition" in subsection 248(1), the rules in amended subsection 107(2.1) apply.

Subsection 107(2) is amended so that it is expressly subject to amended subsections 107(4) to (5). This amendment is made for technical clarity and does not represent any change in policy. Amended subsections 107(4) to (5) describe trust distributions to which subsection 107(2.1) is to apply.

Subsection 107(2) also is amended so that it is subject to new subsections 107(2.001) and (2.002). New subsection 107(2.001) allows a trust to elect out of the rules in subsection 107(2) in respect of a distribution of property to a beneficiary in satisfaction of the beneficiary's capital interest in the trust where

- the trust is resident in Canada at the time of the distribution,
- the property is taxable Canadian property, or

- the property is capital property used in, eligible capital property in respect of, or property described in the inventory of, a business carried on by the trust through a permanent establishment (as defined by regulation) in Canada immediately before the time of the distribution.

If this election is made, the distribution is subject to the rules in amended subsection 107(2.1). An electing trust is generally required to file a prescribed form with the Minister with its tax return for the taxation year that includes the time of the distribution. This amendment applies to distributions made after October 1, 1996. For distributions made before the date of Royal Assent, the election is considered to have been made on a timely basis if it is filed by the filing-due date for the trust's taxation year that includes the date of Royal Assent.

New subsection 107(2.002) applies where a non-resident trust makes a distribution, after 1999, of a property (other than taxable Canadian property or business property connected with a Canadian permanent establishment) to a beneficiary of the trust in satisfaction of the beneficiary's capital interest in the trust. The beneficiary in these circumstances may elect out of the rules in subsection 107(2) in respect of the distribution, with the result that subsection 107(2.1) applies in respect of the distribution. The election is made by filing a prescribed form with the beneficiary's income tax return. Where the election is made, the cost amount of the beneficiary's interest also is deemed to be nil for the purposes of subparagraph 107(1)(*a*)(ii). This amendment applies to distributions made after 1999. For distributions made before the date of Royal Assent, the election is considered to have been made on a timely basis if it is filed by the filing-due date for the beneficiary's taxation year that includes the date of Royal Assent.

Paragraph 107(2)(*b*.1) is introduced (in conjunction with consequential amendments to paragraphs 107(2)(*b*) and (*c*) and the repeal of subsection 107(3)) so that the specified percentages referred to above are explicitly provided under subsection 107(2). This amendment is intended to clarify the operation of subsection 107(2). In addition, the specified percentage for property (other than non-depreciable capital property and eligible capital property) is being increased from 50 per cent to 75 per cent. The specified percentage for eligible capital property is increased from 50 per cent to 100 per cent in recognition that only a maximum of 75 per cent of the cost of eligible capital property can ultimately be deducted for income tax purposes. This amendment is intended to reduce the differential in the tax treatment of depreciable and non-depreciable property in this context, so that this differential corresponds more

closely to that which prevailed before the increase in the capital gains inclusion rate from 50 per cent to 75 per cent.

Paragraph 107(2)(*c*) is amended so that the reduction, because of debt assumed by the beneficiary, to a beneficiary's proceeds of disposition of the beneficiary's capital interest is now provided under the new definition "eligible offset" in subsection 108(1).

Paragraph 107(2)(*d*.1) is amended to clarify the tax consequences of the disposition of taxable Canadian property by a trust to non-resident beneficiaries before October 2, 1996. In the event that the property was explicitly deemed to have been taxable Canadian property under a number of specified provisions of the Act, paragraph 107(2)(*d*.1) ensures that it continues to be taxable Canadian property of the beneficiary. This amendment applies in determining after October 1, 1996 whether property is taxable Canadian property.

Except as indicated above, these amendments apply to distributions made after 1999.

ITA
107(2.01)

Subsection 107(2.01) of the Act allows a personal trust to elect to be treated as if it had disposed of, and reacquired, a principal residence at its fair market value immediately before distributing the property to one of its beneficiaries under subsection 107(2). The rule does not apply to distributions of property by a post-1971 spousal trust in circumstances to which subsection 107(4) applies. (Subsection 107(4) generally applies to distributions made by such a spousal trust to a beneficiary, other than the beneficiary spouse, before the death of the beneficiary spouse.) Subsection 107(2.01) is designed to allow a personal trust to take advantage of the principal residence exemption. In this regard, reference can be made to the definition of "principal residence" in section 54.

Subsection 107(2.01) is amended to eliminate the reference to subsection 107(4), given that subsection 107(2.1) now applies to distributions which amended subsection 107(4) applies.

This amendment applies to distributions made after 1999.

ITA
107(2.1)

Where trust property is distributed by a trust to a beneficiary in satisfaction of the beneficiary's capital interest in the trust and subsection 107(2) of Act does not apply, the rules in

subsection 107(2.1) apply. Subsection 107(2.1) also applies to a distribution by a trust in satisfaction of a right described in subsection 52(6). Under paragraphs 107(2.1)(*a*) to (*c*), the trust is deemed to have disposed of the distributed property for the property's fair market value and the beneficiary is deemed to have acquired the property, and disposed of the capital interest or right described in subsection 52(6), for the same amount. Despite the reference to subsection 52(6) (under which a cost is ascribed to the right to enforce payment out of a trust's capital gains and income), it is unclear that there is relief from double taxation on gains associated with the dispositions of the distributed property and the relinquished capital interest.

Subsection 107(2.1) is amended so that it no longer overrides every other provision of the Act. For example, subsection 107(2.1) no longer deems there to be a disposition of property where the existing law provides that there was no disposition because of paragraph (*e*) of the definition "disposition" in section 54. This amendment is consequential on the replacement of the existing definition "disposition" in section 54 with the new definition of the same expression in subsection 248(1) and new rules in section 107.4 to deal with acquisitions by trusts that do not involve any change in beneficial ownership.

Subsection 107(2.1) is amended so that it applies in connection with all distributions in respect of a capital interest in a trust, regardless of whether the distribution results in a disposition of all or part of the capital interest. This includes rights to which subsection 52(6) formerly applied, but which are now included as part of a capital interest in a trust under the amended definition of "capital interest" in subsection 108(1). However, under amended paragraph 107(2.1)(*c*), proceeds of disposition are only determined with regard to the portion of a capital interest in a trust that is disposed of because of a distribution from the trust.

The proceeds of disposition for the portion of a capital interest in a trust that is disposed of because of a distribution (other than a distribution to which paragraph 107(2.1)(*d*) applies) are determined under paragraph 107(2.1)(*c*) as follows:

- ADD the proceeds of disposition determined in respect of the distribution (other than any portion of those proceeds that is a payment to which paragraph (*g*) or (*h*) of the definition "disposition" in subsection 248(1) applies). Note: paragraph (*g*) or (*h*) of that definition apply to a payment that represents a distribution of income or capital gains or to a payment from a unit trust that does not cause a reduction of the number of issued units of the trust.

- where the property distributed is not Canadian resource property or foreign resource property, SUBTRACT the amount (if any) by which the fair market value of the property exceeds the cost amount of the property (however, disregard this excess to the extent it represents a payment to which paragraph (*g*) or (*h*) of the definition "disposition" in subsection 248(1) applies), and

- SUBTRACT the "eligible offset" in respect of the distribution, as defined in subsection 108(1). (This is essentially debt assumed by the beneficiary on the distribution.)

Where there is no disposition of a capital interest because of paragraph (*g*) or (*h*) of the definition "disposition" in subsection 248(1), an amount distributed from the trust to a beneficiary generally results in a reduction of the beneficiary's adjusted cost base of the capital interest pursuant to paragraph 53(2)(*h*).

Paragraph 107(2.1)(*d*) applies to distributions of property (other than taxable Canadian property or business property connected to a Canadian permanent establishment) from a non-resident trust. In these circumstances, new paragraph 107(2.1)(*d*) deems the beneficiary to acquire the property at its fair market value and to dispose of the corresponding portion of the capital interest in the trust for proceeds equal to the fair market value of the property. Paragraph 107(2.1)(*d*) also ensures that there are no tax consequences to the trust in respect of the distribution of the property.

These amendments apply to distributions made after 1999 (other than distributions before March 2000 in connection with rights described in subsection 52(6) of the Act that were acquired before 2000).

The examples below illustrate the operation of amended subsection 107(2.1). Except as indicated otherwise, it is assumed that the trusts referred to below are all resident in Canada.

EXAMPLE 1

In 2000, a commercial trust distributes non-depreciable capital property (shares) to its beneficiary resident in Canada in satisfaction of the beneficiary's capital interest in the trust. The adjusted cost base of the shares is $40. The adjusted cost base of the beneficiary's capital interest is $20. The fair market value of the property is $100.

Results:

1. Subsection 107(2.1) applies to the distribution.

2. The trust is deemed by paragraph 107(2.1)(a) to have disposed of the property for $100 proceeds, so there is a capital gain of $60 on the resulting disposition and a taxable capital gain of $45.

3. The beneficiary is deemed by paragraph 107(2)(b) to have acquired the property at a $100 cost.

4. Because the distribution gives rise to a capital gain, the amount of the capital gain ($60) reduces the proceeds of disposition of the beneficiary's capital interest under subparagraph 107(2.1)(c)(ii). The beneficiary is deemed to have disposed of the capital interest for $40 proceeds ($100 - $60). Alternatively, in the event that the payment of the gain were considered to be payment of the capital gains of the trust to which paragraph (h) of the definition "disposition" in subsection 248(1) eliminate applied, $40 would be determined under subparagraph 107(2.1)(c)(i) and no amount would be determined under subparagraph 107(2.1)(c)(ii). Consequently, under both of the alternative analyses, the beneficiary's proceeds of disposition of the beneficiary's capital interest in the trust are $40.

5. Consequently, the capital gain from the disposition of the capital interest is $20 ($40 - $20).

EXAMPLE 2

A personal trust distributes non-depreciable capital property (shares that are not taxable Canadian property) to its non-resident beneficiary in satisfaction of the beneficiary's capital interest in the trust. The adjusted cost base of the shares is $40. The adjusted cost base of the beneficiary's capital interest, determined before the application of paragraph 107(1)(a), is $0. The fair market value of the property is $100.

Results:

1. Subsection 107(2.1) applies to the distribution because of the application of amended subsection 107(5).

2. The trust is deemed by paragraph 107(2.1)(a) to have disposed of the property for $100 proceeds, so there is a capital gain of $60 from the resulting disposition and a taxable capital gain of $45.

3. The beneficiary is deemed by paragraph 107(2.1)(b) to have acquired the property at a $100 cost.

4. Because the distribution gives rise to a capital gain, the amount of the capital gain ($60) reduces the proceeds of the beneficiary's capital interest under subparagraph 107(2.1)(c)(ii). The beneficiary is deemed to have disposed of the capital interest for $40 proceeds ($100 - $60). The alternative analysis in paragraph 4 of Example 1 would likewise result in deemed proceeds of $40.

5. The capital interest in the trust constitutes taxable Canadian property for the non-resident beneficiary. For the purposes of computing capital gains, the adjusted cost base of the capital interest under subsection 107(1) is $40, being the greater of its adjusted cost base ($0) determined before the application of that subsection and the cost amount ($40) to the trust of the distributed property. Consequently, the taxable capital gain from the disposition of the capital interest is nil.

6. The allowable capital loss from the disposition of the capital interest is also nil.

ITA
107(2.11)

New subsection 107(2.11) of the Act provides a special rule that, for the purposes of subsections 104(6) and (13), allows income of a trust for a taxation year (computed without reference to subsection 104(6)) to be computed without regard to the tax consequences under subsection 107(2.1) (and former subsection 107(5)) of property distributed in kind to beneficiaries. This ensures that the gains, if any, that might arguably flow-out in some circumstances to beneficiaries as a consequence of the operation of subsections 107(2.1) and (5), will instead be included in income at the trust level.

More specifically, subsection 107(2.11) applies in two cases:

- where a trust resident in Canada distributes property to a non-resident beneficiary after October 1, 1996, the result described above applies in respect of distributions to non-resident beneficiaries if the trust so elects for the taxation year of the distribution or for a taxation year preceding the distribution. The election is considered to have been made on a timely basis if it is filed with the Minister before the trust's filing-due date for its taxation year that includes the date of Royal Assent; and

- where a trust resident in Canada distributes property to a beneficiary after 1999, the result described above also applies in respect of all beneficiaries (including non-resident beneficiaries) if

the trust so elects for the taxation year of the distribution or a taxation year that precedes the distribution. The election is considered to have been made on a timely basis if it is filed with the Minister before the trust's filing-due date for its taxation year that includes the date of Royal Assent.

ITA
107(3)

Subsection 107(3) of the Act is repealed. See the commentary above on amendments to subsection 107(2).

ITA
107(4)

Subsection 107(4) of the Act applies where a post-1971 spousal trust distributes capital property, resource property or land to a beneficiary other than the beneficiary spouse. When this occurs while the beneficiary spouse is alive, there is generally a deemed disposition of the property at its fair market value.

Subsection 107(4) is amended so that similar rules apply to *alter ego* trusts and joint spousal trusts, as newly defined in subsection 248(1). Subsection 107(4) will apply to a distribution by these trusts where the individual (or, in the case of a joint spousal trust, either the individual or the spouse) is alive on the day of the distribution and the distribution is made to a beneficiary other than the individual (or, in the case of a joint benefit trust, the individual or the spouse). For more detail on these trusts, see the commentary on amended subsections 73(1) and 104(4).

Subsection 107(4) is amended so that the rules set out in amended subsection 107(2.1) apply to distributions covered by subsection 107(4).

These amendments apply to distributions made after 1999.

ITA
107(4.1)

Subsection 107(4.1) of the Act applies in certain cases where a reversionary trust distributes property to a specified beneficiary under the trust. When this occurs, there is a deemed disposition of the property at its fair market value.

Subsection 107(4.1) is amended so that, for distributions after 1999 in these cases, the rules set out in amended subsection 107(2.1) apply.

ITA
107(5)

Subsection 107(5) of the Act applies to the distribution of property (other than taxable Canadian property, Canadian resource property and shares in non-resident-owned investment corporations), where the distribution would otherwise be made to a non-resident beneficiary on a rollover basis under subsection 107(2). With regard to such distributions, subsection 107(5) provides for a deemed disposition of the distributed property at its fair market value and an acquisition by the beneficiary for the same amount. In addition, paragraph 107(5)(*c*) provides for proceeds of disposition of the relinquished capital interest equal to the adjusted cost base of that interest.

Subsection 107(5) is amended to replace existing exemptions with regard to taxable Canadian property and Canadian resource property with exemptions for property described in any of new subparagraphs 128.1(4)(*b*)(i) to (iii). This amendment applies to distributions made after October 1, 1996. For further detail on the enumerated subparagraphs, see the commentary on amended subsection 128.1(4).

Subsection 107(5) is also amended so that it only applies with regard to distributions by trusts resident in Canada. This amendment applies to distributions made after October 1, 1996 and recognizes that, if a distribution of the property is made from a non-resident trust to a non-resident beneficiary, Canada's authority to ultimately collect tax on a future disposition of the property has not been compromised because of the distribution. This amendment is consistent with the policy with regard to distributions before October 2, 1996, as the type of property deemed to be disposed of before that date under subsection 107(5) would not have resulted in a non-resident trust being subject to Canadian tax.

Subsection 107(5) is amended so that, where it applies, the amended rules in subsection 107(2.1) provide for the corresponding tax consequences. This amendment applies with regard to distributions made after 1999.

ITA
107(5.1)

Subsection 107(5.1) of the Act is a special rule that applies for the purposes of computing instalment interest. The rule applies where

- there has been one or more distributions after October 1, 1996 of taxable Canadian property by a trust resident in Canada in a taxation year to non-resident beneficiaries, and

- paragraphs 107(2)(*a*) to (*c*) do not apply to such distributions solely because of subsection 107(5).

For the purposes of the measures pertaining to tax instalments or instalment interest in sections 155, and 156, subsections 156.1(1) to (3) and subsections 161(2), (4) and (4.01), the trust's total taxes under Part I and Part I.1 are deemed in these circumstances to be the lesser of two amounts. The first amount is the trust's total taxes payable under those Parts for the distribution year, determined without taking into consideration the carryback of losses and other consequences described in the definition "specified future tax consequence" in subsection 248(1). The second amount is computed in the same manner, except that it is assumed that subsection 107(5) does not apply to each distribution of trust property in the distribution year that is described above. The general effect of subsection 107(5.1) is to ignore a trust's income tax liabilities arising from the distribution of taxable Canadian property to a non-resident beneficiary for the purpose of computing the trust's instalment interest obligations.

Subsection 107(5.1) is similar to new subsection 128.1(5). Both of these subsections should be read in conjunction with new subsections 220(4.5) and (4.6), under which the posting of security can result in a deferral of the accrual of arrears interest on unpaid taxes.

This amendment applies to distributions made after October 1, 1996.

Clause 18

ITA
107.4(1) to (3)

Subsection 107.4(3) of the Act applies where there has been a "qualifying disposition" of property. As set out in subsection 107.4(1), a qualifying disposition of property is a disposition that does not result in any change in the beneficial ownership of the property and that otherwise meets the conditions set out in that subsection. Subsection 107.4(3) generally provides for the rollover of property on the disposition.

To put new section 107.4 in context, the commentary below summarizes the tax consequences of transfers to bare trusts, protective trusts and revocable living trusts under the existing law before describing new section 107.4. Reference should also be made to the commentary on amended section 73 and subsection 104(1).

Bare Trusts

The stated interpretation of the existing law by the Canada Customs and Revenue Agency (CCRA) is that, where property is held by a bare trust, the trust is ignored for income tax purposes and the transferor/settlor is considered to be the owner of property held by the trustee in the trustee's capacity as an agent. Paragraph (*e*) of the definition "disposition" in section 54 is the current authority for the position that there is no "disposition" of property on its transfer to a "bare trust".

The CCRA has stated that it generally views a trust to be a bare trust when:

- the trustee has no significant powers or responsibilities, and can take no action without instructions from the settlor;
- the trustee's only function is to hold legal title to the property; and
- the settlor is the sole beneficiary and can cause the property to revert to him or her at any time.

The CCRA's position that transfers to bare trusts do not constitute "dispositions" has generally been reinforced because, under amended subsection 104(1), "bare trusts" are not treated as trusts. For this reason, the amended definition of "disposition" in subsection 248(1) will not apply because of the transfer by a settlor of a "bare trust" for the benefit of the settlor. In addition, it should be noted that it is possible that a settlor may establish a "bare trust" for another person. Where this is the case, the transfer of property to the "bare trust" by a settlor would be considered to be a disposition of property by the settlor to the person for whom the "bare trust" has been established.

Revocable living trusts

The CCRA has expressed the view that a "revocable living trust" should be fully recognized as a trust for income tax purposes. It is of the view that the transfer of property to such a trust involves a change in beneficial ownership of the property and is at the full fair market value of the property. A "revocable living trust" is an estate planning tool used, instead of a will, by individuals. The settlor of the trust is the trustee and, during his or her lifetime, is the sole income and capital beneficiary and retains the right to revoke, alter or amend the trust at any time. However, there is a change of beneficial ownership involved in a transfer to a "revocable living trust" because other beneficiaries under the trust have rights under the trust in the event that the settlor does not revoke the trust before his or her death.

The draft amendments to section 107.4 are generally consistent with the CCRA's present views in this regard. New subsection 107.4(3) is not intended to apply to transfers to revocable living trusts, on the basis that there is no qualifying disposition of property involved. However, for trusts created after 1999, it is generally possible for individuals who are at least 65 years of age to transfer capital property to a revocable living trust on a rollover basis pursuant to amended subsection 73(1).

Protective trusts

The CCRA considers the attributes of a "protective trust" to be as follows:

- The settlor is the sole beneficiary under the trust.
- The settlor is entitled to as much of the annual income and realized capital gains of the trust as he or she requests.
- The property of the trust will revert to the settlor if the trust is terminated prior to the settlor's death.
- The trust will terminate upon the death of the settlor unless it is terminated at an earlier date. (When the settlor dies, any property held by the trust will devolve in accordance with the terms of the settlor's will or, if the settlor dies intestate, the property of the trust will devolve in accordance with the laws of intestacy that are relevant to the estate.)

The CCRA considers that, under the existing law, a protective trust is fully recognized as a trust for income tax purposes and that there is no "disposition" of property where a settlor transfers it to a protective trust. Trust income and gains are attributed to the settlor in accordance with subsection 75(2).

New subsection 107.4(3) will apply to transfers to protective trusts, assuming that the requirements for a qualifying disposition are met. However, transfers of capital property to protective trusts created after 1999 will generally be covered by amended subsection 73(1).

The rules in subsection 107.4(3) (and subsection 73(1), where it is applicable) also bridge a gap in the existing law in the context of protective trusts by making it clear at what cost a transferee is considered to acquire property where there has been a transfer of property without any change in its beneficial ownership and the bare trust regime does not apply.

New subsections 107.4(1) to (3)

As discussed above, subsection 107.4(3) generally provides a rollover whenever there is a qualifying disposition of property to a trust. Under new subsection 107.4(1), a "qualifying disposition" of property is a "disposition" (as defined in subsection 248(1)) of the property as a result of a transfer to a particular trust where

- because of the disposition, there is a change in the legal ownership of the property that does not result in a change in the beneficial ownership of the property,

- the proceeds would not, disregarding sections 69 and 73, be determined under any other provision of the Act (e.g., transfers from a trust to a beneficiary under the trust where the proceeds are determined under subsection 107(2)),

- the disposition is neither by a person resident in Canada to a non-resident trust nor a transfer of taxable Canadian property from a non-resident person who was resident in Canada in any of the ten calendar years preceding the transfer to a non-resident trust,

- the disposition is not by a partnership (other than a partnership each member of which is non-resident) to a non-resident trust,

- the disposition is not by a partnership, if the disposition is part of a series of transactions or events beginning after Announcement Date that includes the cessation of the partnership's existence and a subsequent distribution from a personal trust to a former member of the partnership in circumstances to which subsection 107(2) applies,

- immediately after the disposition, unless the contributor is a trust, there is no absolute or contingent right as a beneficiary under the particular trust for any beneficiary other than the contributor or joint contributors, as the case may be. (For this purpose, there is a restricted meaning under new subsection 104(1.1) associated with the expression "beneficiary".),

- the disposition does not occur after Announcement Date if the disposition is, or is part of, a transaction where the contributor receives for the disposition any consideration (other than consideration that is an interest of the contributor as a beneficiary under the particular trust or the assumption by the particular trust of debt for which the property may at the time of the disposition reasonably be considered to be security,

- the disposition is not to a trust described in any of paragraphs (*a*) to (*e*.1) of the definition "trust" in subsection 108(1) (generally trusts relating to employee compensation and retirement savings and trusts deemed to exist for income tax purposes), except if it is a disposition by a trust so described,

- the disposition is not part of a series of transactions or events beginning after Announcement Date that includes

  - the disposition of any interest in a personal trust (other than a disposition solely as a consequence of a distribution from the trust),

  - the subsequent acquisition, for consideration given to a personal trust, of any interest in the trust, or

  - the transfer to a trust of property as consideration for the acquisition of a capital interest in another trust, if that property can reasonably be considered to have been received in order to fund distributions from the other trust (other than distributions representing proceeds of disposition of capital interests in the trust),

- subsection 73(1) would not apply to the disposition if no election were made under that subsection and there were no restrictions in subsection 73(1.02) as to the circumstances in which subsection 73(1) applies, and

- where the contributor is an amateur athlete trust, a cemetery care trust, an employee trust, an *inter vivos* trust deemed by subsection 143(1) to exist in respect of a congregation that is a constituent part of a religious organization, a related segregated fund trust (as defined in section 138.1), a trust described in paragraph 149(1)(*o*.4) or a trust governed by an eligible funeral arrangement, an employees profit sharing plan, a registered education savings plan or a registered supplementary unemployment benefit plan, the particular trust is the same type of trust.

Subsection 107.4(2) provides a supplementary rule designed to allow for the division of properties among trusts in certain cases. Consider, for example, the situation where 1000 shares of ABC Corp. are held in trust A for beneficiaries X and Y. Assume that X has a 30 per cent interest in the trust and Y has the remaining 70 per cent interest. If 300 shares are transferred to trust B for X and the remaining 700 shares are transferred on the same day to trust C for Y, there has been no change in the economic interests of X and Y. Subsection 107.4(2) provides that, in these circumstances, the first

condition described above (requiring no change in beneficial ownership) is satisfied provided that trust A receives no consideration. Consequently, assuming the other conditions under subsection 107.4(1) are satisfied, there would be a qualifying disposition of the 300 shares to trust B and another qualifying disposition of the 700 shares to trust C.

Under paragraph 107.4(3)(*a*), the transferor's proceeds from the qualifying disposition are generally deemed to be the cost amount of the property. However, provision is made for the transferor to elect another amount, between the cost amount of the property and its fair market value, as proceeds.

Under paragraph 107.4(3)(*b*), the proceeds determined under paragraph (*a*) are also generally treated as the cost to the transferee trust of the property. However, this amount is reduced in some cases where the fair market value of the property is less than the cost amount. The reduction in these cases is equal to a hypothetical reduction in the transferor's loss on the disposition of the property. This hypothetical reduction is computed, using the stop-loss rules with regard to partnership interests (subsection 100(4)), trust interests (paragraphs 107(1)(*c*) and (*d*)) and shares (subsections 112(3) to (4.2)), on the assumption that the proceeds of disposition are the fair market value of the property rather than its cost amount.

Paragraph 107.4(3)(*b*) does not, however, apply for the purpose of the 20% foreign property limit under Part XI. For this purpose, the cost amount to the transferor under paragraph 107.4(3)(*c*) is the cost amount to the transferee of the same property unless the transferee elects that the cost be the fair market value of the property at the time of its transfer. (It is expected that this election will be used only if the transferee trust does not have information with regard to the cost amount of property from the transferor trust. If, on the other hand, the election is made for the purpose of avoiding Part XI tax, it is invalid.)

In addition, where the property is depreciable property or eligible capital property, there are rules in paragraphs 107.4(3)(*d*) and (*e*) designed, for the purposes of the capital cost allowance rules in the Act, to put the transferee in the same position as the transferor in the event that the transferee subsequently disposes of the property. These rules are parallel to existing rules for trust distributions to beneficiaries in subsection 107(2).

Paragraph 107.4(3)(*f*) provides that, if the property was deemed to be taxable Canadian property of the transferor because of a number of

specified provisions in the Act, the property retains that character in the hands of the transferee.

Paragraph 107.4(3)(*g*) provides that, where the transferor is a related segregated fund trust (as defined in section 138.1), paragraph 138.1(1)(*i*) does not apply in respect of a disposition of an interest in the transferor that occurs in connection with the qualifying disposition. Consequently, no capital loss is provided on the qualifying disposition under paragraph 138.1(1)(*i*) in respect of load fees associated with a policyholder's interest in the transferor. Paragraph 107.4(3)(*g*) also ensures that such amounts can ultimately be recognized on a disposition of an interest in the transferee trust.

Paragraph 107.4(3)(*h*) applies if the transferor was a trust to which property was transferred by an individual (other than a trust) in anticipation of ceasing to reside in Canada and in circumstances to which subsection 73(1) applied. For the purposes of paragraph 104(4)(*a*.3), the transferee trust is likewise deemed to be a trust to which the individual had transferred property in circumstances to which subsection 73(1) applied and in anticipation of ceasing to reside in Canada. Thus, as a consequence of new paragraph 104(4)(*a*.3), there may be a deemed disposition by the transferee trust on the individual ceasing to reside in Canada. Paragraph 107.4(3)(*h*) also applies, where property was transferred by an individual (other than a trust) to the transferor trust in circumstances to which subsection 107.4(3) would apply if no exception under subsection 107.4(1) were made for either transfers to which subsection 73(1) applied or transfers that included the giving to the transferor of any consideration. In these circumstances, the transferee trust is deemed for the purposes of paragraph (*j*) of the definition "excluded personal property" in subsection 128.1(9) to be a trust an interest in which was acquired by the individual as a consequence of a qualifying disposition. Thus, gains with regard to an interest in the transferee trust would be required to be recognized in the event that the individual subsequently ceases to reside in Canada.

Paragraph 107.4(3)(*i*) applies where the transferor was a trust that was neither a personal trust nor a trust prescribed for the purposes of subsection 107(2). In these circumstances, the transferee trust is likewise deemed to be neither a personal trust nor a trust prescribed for the purposes of subsection 107(2).

Paragraph 107.4(3)(*j*) applies where, as a result of a qualifying disposition from one trust to another trust, a taxpayer disposes of the taxpayer's capital interest in the transferor trust and acquires a capital interest in the transferee trust. In these circumstances, the taxpayer is deemed to dispose of the capital interest in the transferor trust for proceeds equal to the cost amount to the taxpayer of that interest.

The taxpayer is also generally deemed to acquire the interest in the transferee trust at that same cost amount. However, the deemed cost amount to the taxpayer of the taxpayer's capital interest in the transferee trust is reduced in some cases where the fair market value of the taxpayer's capital interest in the transferor trust is less than its cost amount to the taxpayer. The reduction in these cases is equal to a hypothetical reduction in the transferor's loss on the disposition of the property. This hypothetical reduction is computed, using the stop-loss rules with regard to trust interests (paragraphs 107(1)(*c*) and (*d*)), on the assumption that the proceeds of disposition are the fair market value of the property rather than its cost amount.

Paragraph 107.4(3)(*k*) applies where the transferor is a trust and a taxpayer's beneficial ownership in property ceases because of a qualifying disposition to be derived from the taxpayer's capital interest in the transferor, but no part of the taxpayer's capital interest in the transferor was disposed of because of the qualifying disposition. In these circumstances, the taxpayer's cost of the taxpayer's capital interest in the transferee trust is increased to reflect the percentage change (attributable to the disposition) in value of the taxpayer's capital interest in the transferee trust. However, the cost amount of the taxpayer's interest in the transferee trust is reduced where the fair market value of the taxpayer's capital interest in the transferor is less than its cost amount to the taxpayer and, had the capital interest in the transferor trust been disposed of, the taxpayer's loss from that hypothetical disposition would have been reduced under the stop-loss rules for trust interests (paragraphs 107(1)(*c*) and (*d*)).

Paragraph 107.4(3)(*l*) generally provides that any amount added under that paragraph in computing the cost to a taxpayer of the taxpayer's capital interest in a transferee trust is deducted in computing the cost to a taxpayer of the taxpayer's capital interest in the transferor. However, the amount of the deduction does not take into account the reduction under paragraph 107.4(3)(*k*) in respect of the stop-loss rules for trust interests.

Where paragraphs 107.4(3)(*j*) and (*k*) do not apply, paragraph 107.4(3)(*m*) deems the cost to the transferor of the capital interest in the transferee trust acquired on the disposition to be:

- where the transferee is a personal trust, nil, and
- in any other case, the excess determined under paragraph 107.4(3)(*b*).

Paragraph 107.4(3)(*n*) applies to a qualifying disposition that is a disposition of a property between two personal trusts. Where,

because of the qualifying disposition, a taxpayer disposes of an income interest (as defined in subsection 108(1)) in the transferor trust and acquires an income interest in the transferee trust, for the purpose of subsection 106(2) the taxpayer is deemed not to dispose of any part of the income interest in the transferor trust. This measure is limited to personal trusts because an income interest only exists respect of such trusts.

These amendments apply to dispositions that occur after December 23, 1998. However, in order to ensure that there will be a cost assigned in certain cases to property previously transferred, these amendments also apply, except for the purposes of Part XI of the Act and Regulations made under that Part, in simplified form to the 1993 and subsequent taxation years. The previous transfers to which the simplified rules apply are transfers (other than transfers to bare trusts) that were not dispositions of property because of paragraph (*e*) of the definition "disposition" in section 54. No proceeds of dispositions are ascribed to these previous transfers and the stop-loss rules in subsection 107.4(3) do not apply.

ITA
107.4(4)

New subsection 107.4(4) of the Act provides a valuation rule with regard to vested capital interests in certain trusts.

For subsection 107.4(4) to apply at any time to a taxpayer's capital interest in a trust, the following additional conditions must be satisfied:

- the interest is vested indefeasibly at that time,
- the trust is not described in any of paragraphs (*a*) to (*e*.1) of the definition "trust" in subsection 108(1), (generally trusts relating to employee compensation and retirement savings and trusts deemed to exist for income tax purposes), and
- capital interests in the trust are not ordinarily disposed of for consideration that reflects the fair market value of the net assets of the trust.

In these circumstances, the fair market value of the capital interest is deemed to be not less than its "share" of the total net assets of the trust. More specifically, the fair market value of the capital interest is deemed to be not less than the product obtained by multiplying the fair market value of the net assets (i.e., assets minus liabilities) of the trust by the proportion of the fair market value of the particular

interest (determined without reference to subsection 107.4(4)) to the total fair market value of all beneficial interests in the trust (determined without reference to subsection 107.4(4)).

These amendments apply to dispositions of capital interests that occur after December 23, 1998.

Clause 19

ITA
108

Section 108 of the Act sets out certain definitions and rules that apply for the purposes of subdivision k, which deals with the taxation of trusts and their beneficiaries. Amendments to section 108 are described below.

ITA
108(1)
"accumulating income"

The amount that may be allocated under subsection 104(15) of the Act to a disabled beneficiary for a trust taxation year is limited to the trust's accumulating income for the year. The trust's accumulating income is designed, in part, to ensure that the preferred beneficiary election cannot be used to allocate income and gains under a spousal trust to non-spouse beneficiaries. Under the existing definition, trust income arising from a deemed disposition of trust assets under subsection 104(4), (5) or (5.2) is not included in computing "accumulating income" and cannot be allocated to beneficiaries in the event that the trust is a spousal trust.

The definition "accumulating income" is amended so that the above restriction only applies in connection with the deemed disposition of trust assets that occurs on the death of the spouse beneficiary under a spousal trust. As a consequence of amendments to paragraph 104(4)(*a*), a similar restriction applies to *alter ego* trusts and joint spousal trusts, as defined in subsection 248(1).

This amendment applies to the 2000 and subsequent taxation years.

ITA
108(1)
"capital interest"

Subsection 108(1) of the Act contains the definition "capital interest". In the case of a personal trust, a prescribed trust and certain

"grandfathered" trusts, a taxpayer's capital interest encompasses all rights of the taxpayer to receive all or any part of the trust's capital. In any other case, a taxpayer's capital interest generally encompasses all rights of the taxpayer as a beneficiary under the trust.

The definition "capital interest" is amended to expressly provide that a capital interest does not include an income interest in the trust. With the exception of an income interest in a trust, a taxpayer's capital interest in a trust encompasses:

- all rights of the taxpayer as a beneficiary under any type of trust, and
- after 1999, a right (other than a right acquired before 2000 and disposed of before March 2000) to enforce payment by the trust that arises as a consequence of any such rights.

This amendment applies after 1999.

Note, in addition, that an amendment to subsection 104(1) has the effect of excluding a "bare trust" from the definition "trust" in the Act. One of the effects of this amendment is that there will be no capital interests in a "bare trust" for the purposes of the Act.

ITA
108(1)
"cost amount"

The calculation of the "cost amount" of a taxpayer's capital interest in a trust is primarily relevant for the purposes of determining a taxpayer's capital gain from the disposition of the taxpayer's capital interest in a personal trust. Under paragraph 107(1)(*a*) of the Act, for capital gains calculation purposes, the adjusted cost base (ACB) of a taxpayer's capital interest is generally the greater of the ACB otherwise determined and the cost amount of the taxpayer's interest determined under subsection 108(1).

Under the existing definition, the cost amount of a taxpayer's capital interest in a trust satisfied by way of a distribution of money is equal to the money distributed. The cost amount of a capital interest satisfied by way of the distribution of other property is equal to the sum of the cost amounts to the trust of those properties. In cases where a capital interest is disposed of without any distribution, the cost amount of a taxpayer's capital interest is considered to be the taxpayer's proportionate share of the trust's money on hand and the total cost amount of other trust property, offset by outstanding trust liabilities. The purpose of the existing definition is essentially to give beneficiaries of personal trusts recognition for cost amounts of trust

assets, given that the cost of capital and income interests in such trusts will generally be nil because of the operation of subsections 106(1.1) and 107(1.1).

The definition is amended so that it does not apply for the purpose of section 107.4. This amendment applies to the 1993 and subsequent taxation years, in order to be consistent with the coming into force for section 107.4.

New paragraph (*a*.1) of the definition is introduced to provide a special rule in the event that an individual is deemed to dispose of a capital interest in a trust immediately before the individual's death. If on the individual's death there is also a deemed disposition of trust assets and an immediate subsequent deemed reacquisition because of the operation of amended paragraph 104(4)(*a*), that deemed reacquisition is considered to occur immediately before the individual's death in order that the "cost amount" of the individual's capital interest reflects the deemed disposition of trust assets. This amendment is intended to prevent double taxation of the same economic gain in these circumstances. This amendment applies to deaths that occur after 1999.

ITA
108(1)
"income interest"

Subsection 108(1) of the Act contains the definition "income interest". It is defined as a right as a beneficiary under a personal trust to income of the trust. Under subsection 108(3), "income" for this purpose is determined without reference to the provisions of the Act.

The definition is amended to provide that, after 1999, an income interest also includes a right (other than a right acquired before 2000 and disposed of before March 2000) to enforce payment by the trust that arises as a consequence of a right that is an income interest.

Except as noted above, these amendments apply in respect of interests created or materially altered after January 31, 1987 that were acquired after 10 p.m. EST, February 6, 1987.

ITA
108(1)
"trust"

Subsection 108(1) of the Act defines "trust". For the purposes of the 21-year deemed disposition rule and the preferred beneficiary election, the definition excludes unit trusts (as defined in

subsection 108(2)) and, except as specified, trusts all interests in which have vested indefeasibly and no interest in which may become effective in the future. One of the specified exceptions from the above exclusion is for trusts described in paragraph 104(4)(*a*) (which, under the existing law, describes only spousal trusts).

The definition is amended so that the above exclusion also applies for the purpose of the rules in section 106 governing the taxation of income interests.

Paragraph (*g*) of the definition is amended so that the exclusion applies to a trust all interests in which have vested indefeasibly (other than trusts described in subparagraphs (i) to (vi) of that paragraph), without regard to whether an interest in the trust becomes effective in the future. However, under new subparagraph (*g*)(v), the exclusion generally does not apply to a trust under the terms of which all or part of any person's interest is terminated with reference to a period of time. The elimination of the requirement that there be no future interest and its replacement by subparagraph (*g*)(v) applies to the 1998 and subsequent taxation years. However, where the trust so elects in writing before its filing-due date for its taxation year that includes the date of Royal Assent (or before such later day as is acceptable to the Minister), these amendments apply only after 2000.

EXAMPLE

A trust provides for beneficiary A to receive income from property for the lifetime of beneficiary A with the remainder interest to go beneficiary B (or the estate of beneficiary B, if beneficiary B does not survive beneficiary A). The above amendment clarifies that the above exclusion from the 21-year rule does not apply in this case. On the other hand, where new units in a trust can be issued by a commercial trust for fair market value consideration, the above amendment ensures that the trust is not precluded from qualifying for the exclusion.

New subparagraph (*g*)(iv) of the definition ensures that the above exclusion does not apply to a trust resident in Canada that has a non-resident beneficiary, unless the total fair market value of the interests of the non-resident beneficiaries is 20% or less of the total fair market value of the interests in the trust. This amendment applies after December 23, 1998.

New subparagraph (*g*)(vi) of the definition ensures that the above exclusion does not apply to a trust that, after Announcement Date, made a distribution to a beneficiary in respect of the beneficiary's capital interest in the trust, if the distribution may reasonably be

considered to have been financed by a liability of the trust and one of the purposes of incurring the liability was to avoid taxes otherwise payable under Part I as a consequence of the death of any individual. This provision parallels new paragraph 104(4)(*a*.2), described in the notes above.

Except as noted above, these amendments apply to the 1998 and subsequent taxation years.

ITA
108(1)
"eligible offset"

Subsection 108(1) of the Act is amended to introduce the expression "eligible offset".

A taxpayer's "eligible offset" in respect of all or part of a taxpayer's capital interest in a trust reduces the taxpayer's proceeds of disposition arising from the satisfaction of all or part of that interest, in the event there is a distribution to which amended subsection 107(2) or (2.1) applies. Where such a distribution was conditional upon the assumption by the taxpayer of a debt or obligation, the taxpayer's eligible offset at any time of in respect of that interest is the portion of the debt or obligation assumed by the taxpayer that can reasonably be considered to be applicable to the property distributed at that time in satisfaction of that interest.

This amendment applies after December 23, 1998. For further detail of the effect of this amendment, see the notes on amendments to subsections 107(2) and (2.1).

ITA
108(1)
"exempt property"

Subsection 108(1) of the Act introduces the definition "exempt property". The expression is used in amended subsections 104(4) to (5.2). For further detail, see the notes above on those subsections.

This amendment applies after 1992.

ITA
108(2)

Subsection 108(2) of the Act describes the requirements for a trust to be a "unit trust" (as defined in subsection 248(1)). A trust must be a unit trust to qualify as a "mutual fund trust" under subsection 132(6).

Paragraph 108(2)(*b*) is amended to allow a trust to qualify as a unit trust throughout a taxation year, provided that at all times throughout the year the trust meets the conditions set out in either paragraph 108(2)(*a*) or (*b*). This ensures that a trust will not lose its status as a unit trust only because it converts from a unit trust described in paragraph 108(2)(*b*) to a unit trust described in paragraph 108(2)(*a*) or *vice versa*.

Paragraph 108(2)(*b*) is intended, because of its closing words, to require a trust more than 20% of the assets of which consist of real property situated in Canada to qualify as a unit trust under paragraph 108(2)(*b*) only if its units are listed on a prescribed stock exchange in Canada. These closing words are replaced by subparagraph 108(2)(*b*)(vi). This subparagraph reflects past amendments to subsection 108(2).

These amendments apply to the 1998 and subsequent taxation years.

ITA
108(3)

Subsection 108(3) of the Act provides that a trust's income is generally its income computed without reference to the provisions of the Act. Subsection 108(3) applies for the purposes of the spousal trust rules in subsection 73(1), as well as other specified purposes.

Subsection 108(3) is amended to change a cross-reference to paragraph 73(1)(*c*) to a cross-reference to new paragraph 73(1.01)(*c*). This is strictly a technical change consequential to amendments to section 73, described in the notes above.

This amendment applies to the 2000 and subsequent taxation years.

ITA
108(4)

Subsection 108(4) of the Act provides that a trust is not disqualified as a spousal trust under a number of specified provisions in the Act merely because of the payment of estate, income or similar taxes.

Subsection 108(4) is amended so that this rule applies not only to spousal trusts but also to trusts established for the exclusive benefit of the settlor during the settlor's lifetime and to trusts established for the joint benefit of the settlor and the settlor's spouse during their lifetimes. This amendment is consequential to changes to section 73 that are described in the notes above.

This amendment applies to the 2000 and subsequent taxation years.

ITA
108(6)

Subsection 108(6) of the Act applies where the terms of a trust are varied. It provides that the application of the 21-year deemed disposition rule is not affected by the variation.

Subsection 108(6) is amended to ensure that no interest of a beneficiary under the trust before it was varied is considered to be consideration for the interest of the beneficiary in the trust as varied. This rule is relevant for a number of specified provisions in the Act, which refer to trust interests being acquired for consideration.

This amendment applies to the 2000 and subsequent taxation years. The amendment is intended to extend to all trust variations, including variations that occurred before 2000.

ITA
108(7)

A "personal trust" is defined in subsection 248(1) of the Act as essentially a testamentary trust or an *inter vivos* trust in which no beneficial interest was acquired for consideration payable to the trust or to a contributor to the trust. An existing special rule within the definition generally ensures that one person (or two or more related persons) can make contributions to a trust and retain an interest under the trust without the prohibition on consideration being considered to apply. This existing rule also applies for the purposes of paragraph 53(2)(*h*), which deals with the calculation of the adjusted cost bases of certain trust interests.

The definition is amended so that this special rule is removed from the definition. Instead, the special rule is now provided in new subsection 108(7). The special rule also is to apply, under subsection 108(7), for the purposes of amended subsection 107(1), strictly as a consequence of the amendments to that provision and for the purposes of paragraph (*j*) of the new definition "excluded personal property" in subsection 128.1(9).

New subsection 108(7) also ensures that, for the purposes of the above-noted provisions, an interest in a trust is deemed not to be acquired for consideration solely because of the acquisition of the interest in satisfaction of any right as a beneficiary under the trust to enforce payment from the trust.

New subsection 108(7) applies after December 23, 1998.

Clause 20

ITA
110.6(12)

Subsection 110.6(12) of the Act generally allows spousal trusts access to the unused lifetime capital gains exemption of the beneficiary spouse, for the taxation year of the spousal trust in which the beneficiary spouse dies. Under paragraph 104(4)(*a*), there is generally a deemed disposition for a post-1971 spousal trust once the beneficiary spouse dies.

Subsection 110.6(12) is amended to ensure that it does not apply to *alter ego* trusts or joint spousal trusts (as newly defined in subsection 248(1)). This amendment is consequential to the extension of paragraph 104(4)(*a*) to provide for deemed dispositions for *alter ego* trusts and joint spousal trusts.

This amendment applies to the 2000 and subsequent taxation years.

Clause 21

ITA
122(2)

Subsection 122(1) provides that *inter vivos* trusts are generally subject to income tax at top marginal income tax rates. Subsection 122(2) of the Act permits certain pre-1972 *inter vivos* trusts access to graduated income tax rates.

Subsection 122(2) is amended to ensure that this special treatment does not apply to a trust in the event that property has been contributed after Announcement Date to the trust from another trust to which subsection 122(1) is not applicable, if there was no change in the beneficial ownership of the property on its transfer.

This amendment applies to the 1999 and subsequent taxation years.

Clause 22

ITA
132(6.2)

New subsection 132(6.2) of the Act is a rule that applies where a mutual fund trust ceases to exist. The taxation year of the mutual fund trust (determined with reference to paragraph 249(1)(*b*)) is not

affected by its termination, unless paragraph 132.2(1)(*b*) applies. Consequently, the last taxation year of a mutual fund trust under the existing income tax rules is generally the calendar year in which it terminates. This leads to unintended consequences under a number of provisions of the Act (including the capital gains refund measure in subsection 132(1), the exemption from the alternative minimum tax in subparagraph 127.55(*f*)(ii) and the exemption from Part XII.2 tax in section 210.1) that require that a trust be a mutual fund trust throughout a taxation year.

New subsection 132(6.2) is intended to address these unintended consequences. A trust that ceases, because it no longer satisfies the 150 unitholder requirement, at any time in a calendar year to be a mutual fund trust is deemed to be a mutual fund trust throughout the year if it was a mutual fund trust at the beginning of the year.

This amendment, which is similar to new subsection 250(6.1), applies to the 1990 and subsequent taxation years.

ITA
132(7)

Under subsection 132(7) of the Act, a trust does not qualify as a mutual fund trust in certain cases where it is reasonable to conclude that the trust was established primarily for the benefit of non-resident persons. The provision's purpose was to discourage the use of mutual fund trusts as intermediaries through which non-residents could invest in Canadian real estate and other taxable Canadian property without recognizing any gains on the disposition of units in trust. However, transitional relief was intended to be provided in the case of a trust which did not issue units after February 20, 1990 otherwise than as a capitalization of an income distribution.

Subsection 132(7) is amended to change references to Canadian real estate, and to specified other taxable Canadian property in section 115, to references to the same types of property in the new definition "taxable Canadian property" in subsection 248(1). This amendment applies after October 1, 1996.

Subsection 132(7) is also amended to ensure that the transitional relief operates as described above. The amendment also ensures that this transitional relief is not interrupted by reason only of an issue of units in satisfaction of payments made out of a trust's capital gains.

Clause 23

ITA
132.11(4) and (6)

Section 132.11 of the Act generally allows mutual fund trusts to elect to have taxation years that end on December 15, rather than on December 31.

Subsection 132.11(4) is designed to permit distributions made in the last 16 days of a calendar year in respect of a trust's taxation year ending on December 15 of the calendar year to be treated as if they were made at the end of that taxation year. Subsection 132.11(6) generally permits a trust that has a December 15 taxation year end to distribute additional income to its unitholders, to the extent that this income is reflected by amounts made payable to these unitholders. Both of these subsections are worded so that rights to these distributions are treated as rights to which subsection 52(6) applies, with the result that there is no capital gain on the satisfaction of these rights.

Subsections 132.11(4) and (6) are amended to reflect the repeal of subsection 52(6) and the introduction of paragraphs (*g*) and (*h*) of the definition "disposition" in subsection 248(1). As a consequence of these paragraphs, there is no disposition (and, as a consequence no capital gain or loss) that arises on the mere satisfaction of the right to enforce payment from a mutual fund trust.

These amendments apply to the 2000 and subsequent taxation years.

Clause 24

ITA
159(6.1)

Subsection 159(6.1) of the Act permits payments of a trust's tax liability resulting from a deemed disposition under paragraph 104(4)(*a*), (*a*.1), (*b*) or (*c*) to be paid (with interest) over 10 years.

Subsection 159(6.1) is amended so that this rule also applies in regard to a trust's tax liability resulting from a deemed disposition under new paragraphs 104(4)(*a*.2) and (*a*.3), described in the notes above.

This amendment applies to the 2000 and subsequent taxation years.

Clause 25

ITA
206(1)
"cost amount"

Part XI of the Act provides a 20% foreign property limit for certain taxpayers, mainly tax-exempt taxpayers such as trusts governed by registered retirement savings plans and registered pension plans. In general, a penalty tax is applied under subsection 206(2) where the total cost amount of foreign property in such a trust or plan exceeds 20% of the total cost amount of all property in the trust or plan.

Where such a taxpayer holds a capital interest in a trust, the income of the trust is usually made payable to the taxpayer so that the income is not taxed at the trust level. Arrangements have been made, however, to "capitalize" income and other amounts payable without having new units issued by the trust. These arrangements are designed to maximize the indirect foreign property holdings for these unitholders by minimizing the cost amount with regard to these capital interests.

Subsection 206(1) is amended to add a special definition of "cost amount" for the purposes of Part XI. The definition is designed to increase the cost amount of a taxpayer's interest in a trust to reflect capitalized amounts payable to the taxpayer. It is also intended to amend Part L of the Income Tax Regulations to make it clear that the definition also applies for this purpose.

This amendment applies after 2000.

Clause 26

ITA
210.2(2)(*b*)

Part XII.2 of the Act imposes a special tax on certain trusts resident in Canada with respect to distributions to certain beneficiaries, including non-resident beneficiaries. The tax is calculated with reference to the trust's "designated income" (as determined under subsection 210.2(2)). "Designated income" is calculated with reference to taxable capital gains and allowable capital losses from dispositions of the trust's taxable Canada property (determined on the assumption that the trust is non-resident).

Paragraph 210.2(2)(*b*) is amended to remove the assumption described above. The amendment merely simplifies paragraph 210.2(2)(*b*) and does not represent any policy change.

This amendment applies after October 1, 1996.

Clause 27

ITA
212(1)(*c*)(i)

Paragraph 212(1)(*c*) of the Act generally provides that a non-resident beneficiary is subject to Part XIII withholding tax on trust distributions in connection with the same types of amounts on which a beneficiary resident in Canada is subject to tax under Part I.

Paragraph 212(1)(*c*) is amended to clarify that the tax consequences of a beneficiary's residence outside Canada will be taken into account in determining the amount subject to tax under paragraph 212(1)(*c*). These tax consequences include the potential indirect tax consequences to a beneficiary of a trust under subsection 104(13) of the application of subsection 107(5) to the trust because the beneficiary is non-resident.

This amendment, which is linked with new section 250.1, applies to amounts paid or credited after Announcement Date.

Clause 28

ITA
248(1)

"personal trust"

A "personal trust" is defined in subsection 248(1) of the Act as a testamentary trust or an *inter vivos* trust in which no beneficial interest was acquired for consideration payable to the trust or to a contributor to the trust. A special rule within the definition generally ensures that one person (or two or more related persons) can make contributions to a trust and retain an interest under the trust without the prohibition on consideration being considered to apply. This special rule also applies for the purposes of paragraph 53(2)(*h*), which deals with the calculation of the adjusted cost bases of certain trust interests.

The definition is amended so that this special rule is removed from the definition. Instead, the special rule is now provided in new subsection 108(7) (as described in the commentary above).

The definition is also amended to expressly exclude, after 1999, unit trusts (as defined in subsection 108(2) of the Act). The reference to unit trusts is being made in this context because under the old definition "personal trust" it was arguable (but by no means certain) that an unusual type of personal trust might technically satisfy the definition "unit trust" in subsection 108(2).

These amendments, and new subsection 108(7), apply after December 23, 1998.

"*alter ego* trust"
"joint spousal trust"
"post-1971 spousal trust"

The new definition "*alter ego* trust" in subsection 248(1) of the Act refers to a trust to which paragraph 104(4)(*a*) would apply if that paragraph were read without reference to subparagraph 104(4)(*a*)(iii) and clause 104(4)(*a*)(iv)(B). Accordingly, for a trust to be an *alter ego* trust it must satisfy the following conditions:

1. at the time of the trust's creation, the taxpayer creating the trust was alive and had attained 65 years of age,

2. the trust was created after 1999,

3. the taxpayer was entitled to receive all of the income of the trust that arose before the taxpayer's death, and

4. no person except the taxpayer could, before the taxpayer's death, receive or otherwise obtain the use of any of the income or capital of the trust.

The definition "joint spousal trust" refers to a trust to which paragraph 104(4)(*a*) would apply if that paragraph were read without reference to subparagraph 104(4)(*a*)(iii) and clause 104(4)(*a*)(iv)(A). Accordingly, for a trust to be a joint spousal trust it must satisfy the following conditions:

1. at the time of the trust's creation, the taxpayer creating the trust was alive and had attained 65 years of age,

2. the trust was created after 1999,

3. the taxpayer or the taxpayer's spouse was, in combination with the spouse or the taxpayer, as the case may be, entitled to receive all of the income of the trust that arose before the later of the death of the taxpayer and the death of the spouse, and

4. no other person could, before the later of those deaths, receive or otherwise obtain the use of any of the income or capital of the trust.

The new definition "post-1971 spousal trust" refers to a trust that would be described in paragraph 104(4)(*a*) if that paragraph were read without reference to subparagraph 104(4)(*a*)(iv). Accordingly, a post-1971 spousal trust must satisfy the following conditions:

1. it is a trust under which only the taxpayer's spouse is entitled to receive all of the income of the trust that arose before the spouse's death, and

2. no person except the spouse could, before the spouse's death, receive or otherwise obtain the use of any of the income or capital of the trust.

Unlike *alter ego* trusts and joint spousal trusts (referred to in the commentary above), a post-1971 spousal trust may also be created by a taxpayer's will.

The definitions "*alter ego* trust" and "joint spousal trust" apply to trusts created after 1999. The definition "post-1971 spousal trust" applies to trusts created after 1971. Other amendments related to the introduction of these definitions include amendments to section 73, subsections 104(5.8), (6) and (15) and subsection 107(4), and the amended definition of "trust" in subsection 108(1). For further detail, see the commentary on those provisions.

"disposition"

The new definition of "disposition" in subsection 248(1) of the Act replaces a definition of the same expression in section 54. The new definition applies for the purposes of the entire Act.

The table below briefly compares the new definition with the former definition, with further detail provided below with regard to the policy changes introduced by the new definition. The first column and second column indicate paragraph references in the new definition and the former definition, respectively.

New	Old	Description
(*a*)	(*a*)	Disposition of property by a taxpayer includes transaction or event entitling taxpayer to proceeds. No policy change.
(*b*)	(*b*)	Specified redemptions, cancellations, conversions and expirations of debt, equity and options treated as dispositions. No policy change.
(*c*)	(*c*)	Except as otherwise specified, dispositions include transfers to and from trusts. No policy change.
(*d*), (*g*) and (*h*)	N/A	Circumstances in which distribution by a trust constitutes disposition of a capital interest in a trust. See description below.
(*e*) and (*f*)	(*e*)	Circumstances in which a transfer not a "disposition" because no change in beneficial ownership. Under the new rules, these circumstances are narrower. See also amended subsection 104(1).
(*i*)	(*d*)	Transfer to secure debt not a disposition. No policy change.
(*j*)	N/A	Other transfers to secure obligations not a disposition. See description below.
(*k*)	(*f*)	Issue of debt not a disposition. No policy change.
(*l*)	(*g*)	Issue of share not a disposition. No policy change.

Transactions involving capital interests in a trust

Paragraph (*d*) of the new definition applies with respect to capital interests in trust. Paragraph (*d*) makes it clear that, except as specifically provided in paragraphs (*g*) and (*h*), every payment (in kind or otherwise) by a trust to a taxpayer in respect of the taxpayer's capital interest (as defined in subsection 108(1)) in the trust will result in a disposition of all or part of the taxpayer's capital interest in the trust.

The exception under paragraph (*g*) applies to a payment made by a trust after 1999 where the following conditions are satisfied:

1. the capital interest in the trust is described by reference to units issued by the trust,

2. the payment does not result in a reduction of the number of units in the trust owned by the taxpayer, and

3. the trust is neither a personal trust nor a trust prescribed for the purpose of subsection 107(2).

The exception under paragraph (*h*) applies to a payment made by a trust after 1999 where the following conditions are satisfied:

1. the payment is made out of the trust's income (determined without reference to subsection 104(6)) or capital gains for a taxation year and the payment was made in the year or the right to the payment was acquired in the year, and

2. the payment is in respect of an amount designated by the trust under subsection 104(20).

Paragraphs (*d*), (*g*) and (*h*) are part of a set of amendments designed to clarify the tax consequences of distributions from trusts to their beneficiaries after 1999. Generally, results achieved under these rules are intended to accord with existing income tax practice. For further detail, see the notes on amendments to subsections 43(2), 52(6), 107(2) and (2.1) and the definition "capital interest" in subsection 108(1).

Transactions involving no change in beneficial ownership of property

Paragraph (*e*) of the new definition provides that there is no disposition where a transfer of property not involving a trust results in a changes in the legal ownership of the property but without a resulting change in the beneficial ownership of the property. This paragraph takes into account past interpretations of the definition "disposition" in section 54. For example, the CCRA has taken the position that there is no disposition where an individual's undivided joint ownership interest in real property is converted to a tenancy-in-common interest in the property.

Paragraph (*f*) of the new definition avoids, unless an election is made to the contrary under subparagraph (*f*)(v), a disposition in the case of certain very simple trust-to-trust transfers involving no change in beneficial ownership. For this paragraph to apply, the following additional conditions must be satisfied:

1. the transfer is not from a trust resident in Canada to a non-resident trust,

2. the transferee does not receive the property in satisfaction of the transferee's right as a beneficiary under the transferor trust,

3. the transferee does not hold property immediately before the transfer other than excluded property. (For this purpose, an excluded property is property the cost of which is included, for the purposes of the Act, in computing a balance of undeducted outlays, expenses or other amounts in respect of the transferee. Thus, an excluded property does not include non-depreciable capital property.),

4. where the transferor is an amateur athlete trust, a cemetery care trust, an employee trust, an *inter vivos* trust deemed by subsection 143(1) to exist in respect of a congregation that is a constituent part of a religious organization, a related segregated fund trust (in this paragraph having the meaning assigned by section 138.1), a trust described in paragraph 149(1)(*o*.4) or a trust governed by an eligible funeral arrangement, an employees profit sharing plan, a registered education savings plan or a registered supplementary unemployment benefit plan, the transferee is the same type of trust,

5. the transfer results, or is part of a series of transactions that results, in the transferor ceasing to exist, and

6. at all times before the transfer or before the beginning of that series of transactions, as the case may be, the transferee held no property or held only property having a nominal value.

Where paragraph (*f*) applies, new subsection 248(25.1) applies with tax consequences described in the commentary on that subsection. Where the paragraph does not apply because the six additional conditions described above are not satisfied, the transfer will generally be a qualifying disposition under new subsection 107.4(1).

Paragraph (*j*) of the new definition also applies to a transfer of property as a consequence of which there is a change in the legal ownership of the property that does not result in any change in the beneficial ownership of the property. For paragraph (*j*) to apply with no resulting disposition resulting from the transfer of property, the main purpose of the transfer must be:

- to provide for payment under a debt or loan,

- to provide comfort that an absolute or contingent obligation of the transferor will be satisfied, or

- to facilitate either the provision of compensation or the enforcement of a penalty, in the event that an absolute or contingent obligation of the transferor is not satisfied.

Where paragraph (*j*) applies, new subsection 248(25.2) applies with tax consequences described in the commentary on that subsection.

Except as indicated otherwise above, these amendments apply to transactions and events that occur after December 23, 1998.

ITA
248(25.1)

New subsection 248(25.1) of the Act applies where there is a transfer of a property from a particular trust to another trust in circumstances to which paragraph (*f*) of the definition "disposition" in subsection 248(1) (explained in the notes above) applies. The result of the application of that paragraph is that the transfer does not constitute a disposition. Where this is the case, subsection 248(25.1) deems the other trust after the particular time to be the same trust as, and a continuation of, the particular trust.

The application of subsection 248(25.1) does not affect the personal liabilities under this Act of the trustees of either trust or the application of subsection 104(5.8) or paragraph 122(2)(*f*).

This amendment applies to transfers that occur after December 23, 1998.

ITA
248(25.2)

Subsection 248(25.2) of the Act applies where at any time there is a transfer of property to a trust in circumstances to which paragraph (*j*) of the definition "disposition" in subsection 248(1) applies. Once the property has been transferred, the trust is deemed to deal with the property as agent for the transferor until there is a subsequent change in its beneficial ownership. However, this rule does not mean that the existence of the trust is disregarded for income tax purposes as the this deemed agency does not apply for the purposes of amended subsection 104(1).

This amendment applies to transfers that occur after December 23, 1998.

ITA
248(25.3)

Subsection 248(25.3) of the Act applies where a trust (other than a personal trust or a prescribed trust) issues particular units of the trust to a taxpayer directly in satisfaction of a right to a qualifying amount payable from the trust in respect of the taxpayer's capital interest in the trust. Where this is the case, the cost to the taxpayer of the particular units is deemed to equal the amount so payable. A qualifying amount payable is one that causes, or but for clauses 53(2)(*h*)(i.1)(A) and (B) would cause, a reduction under subparagraph 53(2)(*h*)(i.1) to the adjusted cost base of the taxpayer's capital interest.

This amendment applies to the 1999 and subsequent taxation years.

Clause 29

ITA
250(6.1)

New subsection 250(6.1) of the Act applies where a trust ceases to exist. The subsection provides that a trust that ceases to exist at any time in a calendar year, and that was resident in Canada immediately before it ceased to exist, is deemed to be resident in Canada during the remaining period in the year. The CCRA takes the position that a trust's taxation year is generally not affected by the termination of the trust. Subsection 250(6.1) is meant to avoid unintended consequences of the CCRA's position that arise under a number of provisions of the Act that require a trust to be resident in Canada throughout a taxation year (e.g. flow-through rules under section 104). Subsection 250(6.1) is similar to new subsection 132(6.2), described in the commentary above.

This amendment applies to the 1990 and subsequent taxation years.

Clause 30

ITA
250.1

New section 250.1 of the Act contain clarifying rules that apply for greater certainty, unless the context requires otherwise.

New paragraph 250.1(*a*) provides that, unless the Minister provides otherwise, the taxation year of a non-resident person is determined in the same manner as that of a person resident in Canada.

New paragraph 250.1(*b*) clarifies that a person who is non-resident at any time in a taxation year is a person for whom "income" for the year is determined in accordance with this Act. It is a non-resident person's "taxable income earned in Canada" that is relevant for the purposes of computing the person's tax liability under Part I. However, a non-resident person does, in some narrow cases, have "income" for purposes of the Act. For example, there are references to a non-resident's "income" (rather than "taxable income earned in Canada") in paragraphs 212(1)(*c*) and 216(1)(*b*) and subparagraph 217(3)(*b*)(ii). In addition, the "income" of a non-resident person may affect the tax liability of a person resident in Canada (e.g., subsection 104(13)).

New section 250.1 applies after Announcement Date.

Clause 31

ITA
251(1)

Section 251 of the Act defines the circumstances in which persons are considered not to deal with each other at arm's length for the purposes of the Act.

Subsection 251(1) is amended to ensure that a taxpayer and a personal trust are deemed not to deal with each other at arm's length if the taxpayer, or any person not dealing at arm's length with the taxpayer, is beneficially interested in the trust. (In determining whether a person is "beneficially interested" in a trust for this purpose, subsection 248(25) is read without reference to subclauses 248(25)(*b*)(iii)(A)(II to (IV) which provide an extended meaning of this expression.) The non-arm's length relationship is relevant, for example, in applying amended subsection 69(1).

This amendment applies after December 23, 1998, but for the purpose of applying the definition "taxable Canadian property" in subsection 248(1) of the Act it applies only in respect of property acquired after December 23, 1998.

Clause 32

ITA
253.1

New section 253.1 of the Act applies for the purposes of subparagraph 108(2)(*b*)(ii) (definition of "unit trust"), paragraphs 130.1(6)(*b*) (definition of "mortgage investment corporation"), 131(8)(*b*) (definition of "mutual fund corporation") and 132(6)(*b*) (definition of "mutual fund trust") and the definition "private holding corporation" in subsection 191(1), where a trust or corporation holds an interest as a limited partner in a limited partnership. Section 253.1 also applies for the purposes of regulations made under paragraph 149(1)(*o*.3) (i.e., section 5101 of the Income Tax Regulations) and paragraph 149(*o*.4) (i.e., section 5001 of the Regulations). These regulations define the expressions "small business investment corporation" and "master trust".

For the purposes of applying the above-noted provisions and definitions where a trust or corporation owns a limited partnership interest, section 253.1 deems the trust or corporation

- to undertake an investing of its funds because of its acquisition and holding of the interest, and

- not to carry on any business or other activity of the partnership because of being a limited partner of that partnership.

This amendment is intended to ensure that the holding of a limited partnership interest by a trust or corporation will not jeopardize the classification of the trust or corporation under specified definitions of the Act and the Regulations. It responds, in part, to the reasoning of the Federal Court of Appeal in *Robinson (Trustee of) v. R.*, [1998] 1 CTC 272, 98 DTC 6065, which, in another context, clarified that limited partners carry on the business of a partnership. As a consequence of this amendment, the meanings of the specified definitions will be determined with reference to new section 253.1 wherever the definitions are used in the Act or Regulations.

This amendment applies after 1992.